

INSURANCE AND THE STATE

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INSURANCE AND THE STATE



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INSURANCE AND THE STATE

BY

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New York

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PREFACE

No more interesting aspect of the public's attitude towards insurance has developed than the opinion which is beginning to be expressed in many quarters that the business should be made a public monopoly. It is difficult to explain fully the origin of this opinion. Perhaps it has its origin in part in the belief by some that the practices of some companies and officials prove that individuals have forfeited the right to conduct insurance as a private business. This may assume that those holding this view have such an understanding of insurance that they perceive its enormous social possibilities and conclude that the possible social uses of it are such that private interests must give way to what they conceive to be a larger public interest. On the other hand, the opinion may be a result of the conviction which many have come to have that the state should be intrusted with any activity which affects large numbers of its citizens. This assumes a faith in the efficiency and integrity of public officials which many do not yet hold.

PREFACE

The author hopes that his practical experience in the business and his teaching of the subject have made it possible for him to appreciate the arguments of the opposing parties to the controversy. This brief discussion is modestly offered in the hope, therefore, that it may be of some value in modifying the extreme views on each side and aiding others in reaching a rational conclusion. If the discussion has any value, it must be because of the questions which it raises and not of those which it answers.

No effort has been made to write a brief either for or against a state monopoly of insurance. Many of the statements will doubtless seem absurd to one or the other class of extremists, but it is hoped that there is a large class who are open minded and will find something in the discussion to aid them in arriving at a rational conclusion.

Insurance as a subject for formal study and writing has received surprisingly little attention in the United States, notwithstanding the fact that it has had in this country a wonderful development and has been a subject for frequent legislation and investigation in the numerous states.

Practically no one except those interested in

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selling insurance and managing the companies has given the business the study which its importance demands. This condition has been unfortunate both for the public and the insurance business. Those connected with the companies came to have in many instances little respect for the public's knowledge of insurance and sometimes little consideration for the public interest involved in the conduct of the business. Practices in the formation and operation of companies were thus made possible which have injured the insurance business, partly because of the practices themselves and partly because of unwisely enacted laws. As the public became interested in the methods of business conduct, attention was directed to the insurance business with the idea of instituting certain reforms. Yet when the public endeavored to apply the reform ideas to this business, it was found that few legislators had the knowledge which was necessary to direct constructive reform legislation. Insurance in its fundamental aspects is not like other business in that it is not one for great private profit. Yet as it had been practiced in many instances it had become of this character, and hence many legislators classed it with the ordinary private business. It

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seemed to the legislator a proper source of revenue for the treasury, a business to be placed under the anti-trust laws and a business to be discriminated against in one state when it was organized in another state. The insurance class was distrusted as a source of information upon which to base legislation. The result has been that legislation has sometimes been enacted from which the business and ultimately the public have suffered.

It is hoped that the reader will find in these pages a fair discussion of the diverse views of legislators and the insurance fraternity and that some light may be thrown on the question of the proper relation of the state to the insurance business. In our present day zeal for state direction of activities formerly of a private nature, our confidence in the state as an agent may precipitate us into lines of action before adequate study and preparation have been made. Success in collective action as in individual action cannot be predicted upon following prescribed rules of procedure which are good for all times and for all peoples.

The data for the statistical tables and calculations have been taken from the Spectator's Annuals, State Insurance Reports, the United States Census, and Brown's Book of Life Insurance Economics.

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The first named reference has been of especial value. Caution has usually been given against making the statistics prove too much. Insurance statistics are peculiarly susceptible of being strained to prove a point.

W. F. GEPHART.

OHIO STATE UNIVERSITY,

March 1, 1913.

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CHAPTER I

THE CHARACTER OF INSURANCE AND ITS LEGAL STATUS

ALL human progress which is essentially an increase in social well-being has arisen from some improved method of coöperation, whether this new form of coöperation has resulted from private initiative or from public compulsion in obedience to enacted law. There is probably no other form of coöperation which is so fundamentally valuable to the coöperative members, indiscriminately, rather than to particular members, than insurance. In insurance is found every essence of coöperation. It is therefore proposed to examine the character and status of insurance as a business, upon what may be called the eve of the experiment of directing this form of coöperation by the state rather than by the initiative of

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private individuals. Everywhere in the United States, with certain minor exceptions to be discussed later, the business of insurance is under private control. It is also a business subject to the control of the various states of the Union, since the Supreme Court of the United States has decided in a very definite manner that it is neither interstate commerce nor an instrumentality of commerce. Hence it is not under the control of Congress; at least it does not fall under that section of the Constitution which gives to Congress extensive powers of controlling interstate and foreign commerce.

Although the federal government may exercise some power over insurance by an exercise of the taxation power, yet this power is concurrent with a similar power of the states, and the larger powers of regulation are limited by the decisions of the federal supreme court. It therefore appears that the subject of insurance will continue to be one over which the states will exercise major control. An examination of the present statutes in force in the various states on the subject of insurance discloses great variation in the laws. Some desirable uniformity has been accomplished within the past decade, but lack of uniformity is the

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chief characteristic of state laws affecting insurance. This condition gives no promise of change. The business is essentially interstate; that is to state, the greater percentage by far of insurance in force on the books of the companies is composed of policies from more than one state. Yet the legislature of each state persists in treating the business as a purely state business. Most of the legislatures attempt to favor, as they imagine, home companies, notwithstanding the fact that it is usually the practice of a home company only to confine its business to the state until it gets under way as a going concern. It is true that the small local mutual companies restrict the territory of operation, but every important life and property insurance company in the United States does business in other than the state of its incorporation. This confusing, burdensome, and inequitable legislation takes various forms. It may be and is generally true in the case of the taxes levied on insurance. One state may levy $1\frac{1}{2}$ per cent on gross premium receipts collected in the state, another 2 per cent on the same, and still another 1 per cent on the net premium receipts. One state may lay down in great detail provisions regarding the formation of a company and the

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sale of its stock, while another state may have few provisions in its laws regarding the subject. One state may attempt "to keep money in its borders" by requiring a large percentage of the premiums received in the state to be locally invested, while another may permit the fullest liberty of investment, not only as to the principal sums collected, but also as to the kind of securities in which the sums may be invested.

The development of insurance, not only as to the increase in the numbers of policyholders of the ordinary kinds of insurance, but also as to new applications of the insurance principle, that is, new kinds of insurance, has been greatly hindered by this burden of confusing legislation. It has added enormously to the cost of insurance to the policyholders, and it has made adjustments to new conditions difficult. New forms of insurance have slowly arisen in the United States as compared with the European countries, but it is not due chiefly to the fact that the insurance officials have been less inventive or skillful. The wonderful accomplishments which have been secured in the old established lines of insurance give some idea of what might have been secured if the business had not been hampered by restric-

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tive and confusing state legislation. As it is, voluntary insurance in America far exceeds in number of policies and volume of insurance all that of the remainder of the world.

Before the problem of state insurance is considered in detail it will be well to examine the character of insurance as a business. Does its administration present difficult problems? Is it a business fraught with great public or social importance? Insurance, as has been stated, is a method of coöperation. It is the joining together of a number of individuals necessarily exposed to a risk for the purpose of collectively assuming and therefore distributing a risk otherwise borne by the individual. The total risk assumed under insurance is less than the sum of the individual risks borne previous to the application of the insurance principle. This is true because a larger degree of certainty is exchanged for uncertainty, inasmuch as the benefit of the law of average is secured. The application of the insurance principle presents no great difficulties. That is to say, in most forms of insurance the basis upon which the operation is made is well understood. The principles have been established from the study of data and experience. Insurance is, in

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other words, in most branches thoroughly scientific. There is no great risk to be assumed by the organizers. In life insurance the mortality statistics are, as a whole, sufficiently accurate to assure that the insurance given under them carries no risk to the insurer. In fire insurance the burning rate is fairly well known. In other kinds of insurance the data may not be either as complete or as accurate, but few inherent difficulties will be found in placing in operation the insurance principle. Insurance is, in other words, a safe business. It is not complex. It is relatively simple so far as the fundamental principles upon which it is based are concerned. Problems indeed do arise in the administration of the business; such, for example, as the investment of the funds advantageously and safely, and the equitable determination of charges as regards different individuals, but these facts do not disprove the original statement that the principles underlying the business are well understood and that it is relatively easy to place them in operation. Therefore for the state to assume the business of insurance would not involve its entering upon new, untried, and dangerous grounds. Is it a business fraught with social import? If insurance is a

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method of assuming and distributing necessary risks, it must have great social importance. If death, sickness, accidents, and destruction of property are risks to which every one in some form is subjected, then any means whereby the risks are reduced must have great social value. It is urged by some that such is the social value of the utilization of the insurance principle that the members of society should not be permitted to decide voluntarily whether or no they shall avail themselves of the principle, but should be forced to do so. It is undoubtedly true that no one can escape the risk, and no means of reducing the risk is known, other than that of using the insurance principle. However true this may be, it does not follow as a consequence that the state should necessarily assume this business.

At this point arises the unanswerable question of what should be the function of the state. Upon what principles shall the sphere of state activity be decided? The once generally accepted principle, that the state should not do for an individual or group of individuals what they could equally as well do for themselves, gives us no great aid in deciding the question. With the increasing development of democratic ideas the state has come to

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be considered an organ for the expression, protection, and development of social needs as distinguished from individual or group interests. Nor is the state to be solely an organ for serving the present generation, but it is more and more to be used to prepare the way for the future generations. It is maintained that the social well-being to be furthered by the state is therefore something more than the sum total of the individual well-being of the present living, and that even if the present well-being alone is considered, a unified activity of the state brings greater benefit to all than the same activity diversified by remaining under the control of private individuals.

↓ New fields of state activity are continually being found with that increased complexity of society which calls for the nicer and nicer adjustment of one's conduct towards his fellows which can only be secured under the single directing and unifying organ of society — the state. The fact that in the United States there are many obstacles to this increased activity of the state, such as constitutions, need cause no great concern. Such obstacles must be trivial and temporary when a long, distinct vision of society is taken. Already the people are forming the habit of amend-

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ing and revising constitutions or adopting entirely new ones in the states, and as they more and more realize their sovereignty they will fashion their tools, like any good workman, to do the work which they wish them to do. So far, then, as they realize that a constitution and the laws which are made under it are but expressions of the will of the people, so far will they change their past expressions to suit present ideas. Constitutions and laws therefore present but temporary obstacles to the assumption or even monopolization of the insurance business by the state.

It may now be inquired if the business of insurance is of a kind which is suitable for a source of private gain; that is to state, is it a business from which individuals should be permitted to take profit in the technical sense of the word? Or is it a business of such social importance that its costs to those whom it serves should be prime costs? That is, should the outlay for the service be limited to wages for those who are employed to conduct the business of insurance? Even conceding a monopoly of this business by the state, it would probably not mean a great reduction in the number of wage earners who are now employed in the business. But it certainly would mean

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that the business of insurance would afford no opportunity to the capitalist for the employment of capital and but a very limited opportunity for the landowner to secure rent, because insurance under government operation would be purely mutual insurance, or if it should be administered on a basis for profit, the surplus would go to the state treasury.

Whether it is or is not a suitable business for profit must be determined largely by two considerations. First, to what extent is the individual free to deal in the commodity or service? Second, to what degree is the element of risk present whereby unusual skill, foresight, and great ability are under our present economic system supposed to justify one in taking or receiving a large return in the nature of a profit, risk interest, wages of management, or whatever we are pleased to call this unusual fund?

As to the first point, we have but to consider again the nature of insurance. It is but a method of assuming and distributing necessary risks to which every one is in some manner exposed. The fact that many do not avail themselves of the insurance principle does not prove that they are essentially free to choose. Indeed they have

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chosen. The risk remains whether or not they choose to admit its existence. Their failure to reduce the risk by joining with their fellows in applying the insurance principle means that their social mind lacks development, and it means further that their fellows ultimately bear a large part of the risk. The loss of a life is usually a loss to society, not only because of the potential value of the life itself, but also because of the withdrawal of protection from those dependent upon that life for support and preparation for efficient living. The loss of a property falls immediately upon the owner, but it is also a destruction of so much social capital. The loss of time by sickness or accidents means that so much less of the work of the world is done, or perchance it is shunted upon shoulders already heavy with work. The individual ought not to be free to choose whether he shall increase social well-being by using the insurance principle, even though it be true that insurance *per se* gives but a very indirect benefit to the individual. Its first and fundamental characteristic is mutuality; the principle of each for all and all for each. If, then, the idea of profit to the insured is excluded by the very nature of insurance, and if it is a method of reducing nec-

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essary risks and if the value resulting is distinctly a social value, should individuals be permitted to receive a profit from administering it? Paradoxical as it may appear, it is the insurance officials who unconsciously argue for this view. This is most clearly shown in the taxation laws of the various states. The greater number of insurance officials, especially those connected with the life insurance companies, oppose the taxation of insurance on the ground that its character does not justify the tax. It is called by them a "tax on thrift," yet the legislators make insurance a source of considerable revenue for the state.

As to the second point, viz. whether there is such a risk present in conducting the business as would justify the taking of a profit. This question has been answered in part by the consideration of the basis or principles upon which the business is conducted. These principles have been in most kinds of insurance long known and well understood. The results of many years' application of the principles are known. The data are available, and in most cases are organized or capable of being organized, so that no great element of risk is present. This is not to state that perfection has been reached in applying these

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data, but certainly with our present knowledge there is no excuse for dangerous experiments. Mortality and morbidity statistics are available and are becoming more accurate. Marine and fire insurance experience extends over a long series of years. The costs of insurance are well known, or at least we know that a certain minimum amount must be collected. How much less might be sufficient is a debatable question, but there is no necessity to answer that question in the event the state should decide to monopolize the business. In short, the application of the insurance principle presents no great difficulties or risks. It is not a venture upon unknown seas.

CHAPTER II

STATE INSURANCE IN PRACTICE

IT does not follow from the preceding description of insurance that great ability and skill are not required to administer the business. Nothing could be farther from the truth. Not only is great organizing ability required, but also great financial ability is demanded in investing and caring for the enormous trustee funds. It may be argued that it is in connection with the investment of these funds that the element of risk appears which justifies the profit to the individual. But an examination of the interest rate assumed and actually earned, together with the course of the interest rate during the past centuries and a study of its probable range in the future, removes any great doubt on this point. Very few of those who receive either interest or profit from the insurance business would be bold enough to maintain that this was a return either for the risk they had assumed or for their great foresight in

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investing insurance funds. Before considering in detail the problems of state insurance of each of the kinds of insurance, a description of what has already been done by the different nations in state insurance will be of value.

The most notable case of state insurance is that established by the Italian law of April 4, 1912. This law makes life insurance a state monopoly. The issuing of all policies of life insurance is intrusted to a National Institute of Insurance, a department of the state to which the treasury of the state issues the money necessary for its operation. The net profit of operation goes to the public treasury for a fund to provide working-men pensions. However, it is not primarily financial in its purpose; for, as Minister Nitti insists, "the essential thing is not to obtain revenue for the state, but to render life insurance popular with the classes and to make it accessible to all." It must be emphasized that whatever profit results does not go to pay the normal expenses of the state, but is to be set aside *in toto* for the specific social purpose of providing pensions for workingmen.

It is to be especially noted that the law applies only to life insurance, and even in this case the

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social aspect of such insurance is recognized by exempting the following classes of life insurance organizations: (a) Provident Institutions authorized by law to the service of pensions or annuities. (b) Banks of Providence recognized by royal decree. (c) Mutual societies the aim of which is not speculation and which insure their members for a sum not in excess of 1000 lire or pay an annuity not to exceed 400 lire. (d) Public and private institutions which directly grant pensions, rewards, or aid at the time of death of their employees. (e) Life annuities stipulated and acceding to the Articles of 1789 and following the Civil Code. The law nullifies all contracts of life insurance made after the law of 1912 is placed in effect and denies a hearing in Italian courts on insurance contracts made in foreign countries. It is made an offense for a company or its agents to solicit life insurance, and in case this is done, the agent is fined, the contract is nullified, and the informer is given a part of the fine.

All tontine and annuity companies are prohibited, and the present business of such companies, either foreign or domestic, must be liquidated. The law requires each company having

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insurance policies in force to file with the government a detailed statement of each policy, and all such policies not so scheduled are declared null and void. Each policyholder is requested to see that the company so declares his policy, and if the company has not done this, the policyholder must. It has been decided to grant a certain number of years during which the transfer from private to state insurance may take place without causing too much damage. This interval also gives time for the National Institute to prepare itself to function properly.

The following principles govern the relationship between the new state and the old private insurance.

(a) No indemnity of any kind will be given to the private insurance companies, either domestic or foreign. Italy has no constitution. All laws are constitutional, and the Italian courts have no choice but to apply the law. Foreign companies, therefore, can have no indemnity granted by the Italian courts. What will be the result of the request which has been made by some of these foreign companies to their departments of state to take up the subject with Italy is a matter of conjecture. Such a question might

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reach the Hague Tribunal, and if an award in favor of the foreign companies were granted, an embarrassing situation might arise. If foreign companies were indemnified, certainly the Italian companies should also receive indemnities.

(b) During a period not to exceed ten years existing companies may continue to do business under certain restrictions. Some of these restrictions are that the company must turn over 40 per cent of every risk to the National Institute; within thirty days after writing the risk the company must send to the Institute a full description of the risk and give it an opportunity to accept or reject the risk. If the Institute accepts the risk, it becomes a creditor for a part of the premium to cover that part of the risk assumed.

(c) All companies foreign or domestic may call upon the Institute to assume all its contracts of insurance written previous to Dec. 31, 1911. Companies continuing business under the ten-year limit can surrender their business at any time. The Institute must accept the business if the proper reserve is held on the policies.

(d) If contracts are not surrendered, they must be executed the same as if there was no state monopoly.

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The National Institute of Life Insurance has a legal and financial autonomy. It is a public service under inspection, with provisions to exclude politics from its operation. It has its own budget, although the state guarantees the obligations assumed. The capital of the Institute is exempt from taxation, but the contracts of insurance are taxed. It has the postal and telegraph franchise. In addition to the administrative officials and office force, agents are employed who are paid on a commission, proportional to the amount of the business secured. All persons actively engaged or interested in politics are forbidden to hold any administrative positions, and in addition certain qualifications for the particular position must be possessed. The tenure of office is also secured.

Switzerland, after a referendum vote, passed a law June, 1911, which provides for a state monopoly of insurance against accidents and sickness. In addition certain cantons have government insurance against different risks. Some of them provide insurance against fire. This insurance is compulsory. The canton of Neuchâtel has public life insurance. These various forms of public insurance do not, in most cases, provide

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for a public monopoly of the business. They compete with the private companies for business. In several of the German states public insurance is also found, but in no case is a monopoly of the business established. Bavaria, for example, has public insurance against fire, live stock, and storms. The German plan of workingmen's insurance by the imperial government will receive consideration later. In Norway public insurance against fire and accidents is found, but not as a monopoly. In Belgium and other European countries other examples of public insurance are found. The recently enacted National Insurance Law of England needs only to be named to call attention to this far-reaching experiment in state insurance. England has offered for many years industrial insurance through its post-office organization. Annuities have also been offered for many years without securing large results. In France state insurance is one of the most important questions of the day. During the last several sessions of the Chamber of Deputies bills have been introduced organizing a state monopoly of insurance, and important officials of the various governments of late years have declared themselves in favor of the plan so soon as a means of realizing the work

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can be devised. There exists already public insurance in France against accidents and fire, but these are without a monopoly. In some of the Australian states, especially New Zealand, life insurance by the state is provided, but here also it is found in competition with private companies.

The United States also affords various examples of state insurance, the most interesting of which is probably the plan recently placed in operation in Wisconsin. The law passed by the legislature of 1911 provides for the sale of life insurance policies by the state, beginning Jan. 1, 1913. The law provides for a life fund beyond which the state is not responsible. The state treasurer is custodian of the fund, and all other matters in relation to the sale of the insurance are under the supervision of the commissioner of insurance. The premiums are based upon the American experience table of mortality with interest at 3 per cent. The net premium thus provided for has added to it as a loading two dollars per year per thousand dollars of insurance and "an amount distributed equally through each of the possible premium payments, the present value of which shall be equal to one sixth of the present value of the costs of insurance on the basis aforesaid";

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that is, one sixth the present value of the net natural premium for that year's insurance.

The factory inspectors of the state, the clerk and treasurer of every county, town, city, and village, and even state banks are made agents, and it is the duty of each to transmit to the insurance departments applications, when requested to do so. The commissioner of insurance and the state board of health pass upon all applications after a medical examination by a local physician has been made. The law provides for the accumulation of a surplus which is made up of 50 per cent of the net profits on each policy for the first year, and thereafter 5 per cent less for each succeeding year until the ninth year, and thereafter 10 per cent of such profit during the continuation of the policy. The interest on this surplus fund also becomes a part of this surplus which is to be held "to meet losses from unexpected or great mortality, or depreciation in securities or otherwise." The remainder of the profits are distributed annually to the policyholder. No revenue is sought by the state, but the expenses of transacting the business are to be met from the life fund. Any person is authorized to transmit applications for insurance to the state department, for which a

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fee of twenty-five cents is paid. Likewise a fee of 1 per cent is paid for collecting and transmitting any premium, and such a person is held to be the agent of the insured. Similarly the individual may transmit his own application or premium and retain twenty-five cents or 1 per cent of the premium. Policies of life insurance are issued under most of the ordinary forms sold by private companies, but are in a sum of \$500 or multiples thereof up to \$1000 on a single risk until the number of insurants equals 1000, to \$2000 until the number insured reaches 3000, and then not in excess of \$3000 on a single life. The age limits are fixed at twenty and fifty years. It will thus be observed that the plan provided is conservative.

The premium rates are less than those charged by private companies for the same kind and class of policy. This is especially true in the case of endowment policies, where the difference in the short-term endowments is as much as \$10. In the case of a ten-year endowment at age thirty-five the loading in the state rate is only \$2.77. Other aspects of the plan will be discussed when the detailed problem of a state monopoly of life insurance is considered.

The Massachusetts plan of Savings Bank In-

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surance is not a pure example of state insurance, but it has some characteristics of state insurance. Under the law of 1907 savings banks under certain conditions were authorized to sell contracts of insurance and annuities, the former granting indemnity in case of death not to exceed \$500, and the latter paying in any year not more than \$200. A special guarantee insurance fund must be provided for the above purposes. The General Insurance Guaranty Fund is created a body corporate, the affairs of the corporation being managed by a board of seven trustees appointed by the governor from the list of the trustees of savings banks and insurance banks. Only residents of the state can be insured under this law. No solicitors or collectors can be employed. The expenses of the actuarial, medical, and other services are borne by the state. The results achieved under the law are indicated by the following table:—

YEAR	NO. OF SAVINGS BANKS WITH INSURANCE DEPARTMENTS	NO. OF POLICIES	AMOUNT OF INSURANCE
1908	2	282	\$114,953
1909	2	2513	992,761
1910	2	3318	1,367,363
1911	3	5063	1,956,038
1912	4	6652	2,528,809

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These banks have established agencies at various places in the state in savings banks, trust companies, stores, Y. M. C. A.'s, high schools, and memorial institutes, where application for insurance may be made and premiums paid. There are also two hundred unpaid agencies in mills and factories for the benefit of employees only.

The total premium income for 1911 was \$102,-832.27 and the total disbursements for the year \$39,644.37, of which \$21,877.67 was to policy-holders. This sum was divided as follows: \$6513 for death claims; \$7117.71 as dividends; \$5850.04 as surrender values; and \$2189.19 as surrender values, used to buy paid-up insurance. The expenses for the year chargeable against the premiums were about 17.3 per cent, and the ratio of expense against the premiums after the first year was about 14 per cent. Notwithstanding this favorable showing and notwithstanding the numerous opportunities given to the public to purchase the insurance, the fact that only four savings banks and 6652 persons have in five years used the plan will be held to be by some strong indication of the final failure of the plan.

The foregoing are then the chief examples of state insurance, with the one remaining exception

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of the state insurance for industrial accidents. The European countries again supply many examples in this particular, but this form of state insurance is also being rapidly adopted in the states of the United States. Probably the Ohio plan is typical of what is attempted.

The law of 1911 created a state insurance fund for the purpose of granting indemnity to injured workmen. The law is not compulsory, and it affects only employers who employ five or more operatives regularly in the same business. The expense of administering the fund is borne by the state. If an employer does not avail himself of the provisions of the law, he is denied setting up as a defense, in case of a suit, the defenses of assumption of risk, fellow servant, or contributory negligence. Compensation is provided in the case of all injuries received in the course of employment without regard to the question of negligence, except that no compensation is allowed for an injury which has been self-inflicted. The compensation received in case of injury is from \$5 to \$12 per week unless the wage is less than \$5 per week, with the provision that compensation shall not continue for more than six years and that the total sum received shall not

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exceed \$3750. If permanent total disability is suffered, similar payments are made during the lifetime of the injured employee. In case of death the dependents of the workmen are paid certain sums, depending upon the wage received. The fund is administered by a board of awards, which is given very large powers. The employers pay 90 per cent of the premium and the employees 10 per cent, the premium being based upon the accidents of the industries according to the classification made by the board.

As amended in 1912, the law compels the employer to pay all the premium or cost of the insurance. A more important amendment was to make it practically compulsory for all employers of five or more workmen to insure with the state board rather than with the private company. The employer still has the privilege of refusing to take any insurance, but if he does, he is deprived of setting up as a defense any of the old common-law defenses. But if he insures, it must be with the state department, established for this purpose. There is only one exception. An employer or a mutual association of employers may provide the indemnity specified in the law, but in this event, he or they must submit to strict super-

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vision by the State Board of Award. A bond for the security of the payments of the compensation must be given to the Board, and at all times the employer or the association must submit to the detailed rules laid down by the Board. In the case of self or mutual insurance a contribution must be made to the surplus fund which the Board is required to accumulate. This surplus fund is made up of 10 per cent of all premium receipts until the fund reaches \$100,000 and then 5 per cent of such receipts until such time as the Board has decided that the surplus is sufficiently large.

Another important provision was to make the insurance compulsory on the state, county, city, township, incorporated village, and school district; that is, it is compulsory compensation for public as well as private employees.

Rates are based upon a classification of occupations with respect to their hazards, the pay roll, and the number of employees. It is the duty of the Board to ultimately fix and maintain the lowest rates possible for each class of occupations, consistent with the maintenance of a solvent insurance fund, the creation and maintenance of a reasonable surplus. Rates are adjusted semi-

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annually, and if the experience in an industry or a plant shows that an unnecessarily high rate has been collected, the excess in it is credited to the future premiums due from the employer.

CHAPTER III

SHOULD THE STATE MONOPOLIZE LIFE INSURANCE?

IT may now be inquired after this survey of the examples of state insurance as to the grounds upon which such activity of the state may be based. It will aid to a better understanding of the question, if the consideration is taken up under the following three divisions:—

(1) What considerations should cause the state to assume, either in competition with private companies or as a state monopoly, the business of life insurance?

(2) Would the same reason apply in the case of fire insurance?

(3) Would the same reasons apply to the miscellaneous lines of insurance, especially to sickness and industrial accident insurance?

If the state assumes the business of life insurance, it must be for one or more of three reasons:—

(a) As a desirable source of securing revenue for the state.

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(b) As a social developmental activity whereby greater numbers may benefit from an application of the insurance principle.

(c) As a method of completely regulating the business without the primary object either of revenue or of extending its social benefits.

On the first point it may be questioned if life insurance is a proper source of revenue for the state. It is, as has been shown, a means of providing a common need. It is an indemnity in part for the loss of life. It can be neither a speculation nor a source of profit for him who buys it. Its possession yields to him no income. It is property without revenue-yielding power in the possession of the holder, although this characteristic is lost when it becomes the property of the beneficiary; but it is not then insurance. It is the proceeds of insurance. Whatever revenue the state collects is collected for a public purpose; that is, it is to be expended in furthering social well-being in some form. Therefore the collection of funds from the sale of insurance would logically imply that these funds were to be expended for a social purpose, not of equal importance to insurance, but superior to it.

No other characteristic of political thought is

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more significant at present than the remarkable growth of the idea that the state is an institution of the people, and as such should be used to further the interests of the masses. With this growing democratic conception it is difficult to imagine that the people would consent to the use of such a distinctively social institution as insurance for the purpose of financing other interests of the state. In the United States, where practical democracy is gradually taking the place of theoretical democracy, such a use of insurance is scarcely conceivable. A democratic constituency of an elected representative would not consent to such an antisocial use of insurance, and because they are a popular electorate, a powerful weapon for enforcing the wishes of the people would be in their possession by means of their voting power.

How large such a possible revenue would be would depend upon such factors as the rates charged for the service, and the outlays for conducting the business. In 1911 the ordinary Life Insurance Companies in the United States had a capital of \$46,712,523. The capital stock is in many cases, as in Mutual Companies, only that nominal sum which is required by the state laws.

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The dividend paid on this capital stock was 4.3 per cent. The total admitted assets were \$4,164,-491,688, and the income from all sources during the year was \$836,160,804. There was paid out for agents, other employees, and operating expenses \$165,614,119.

The dividends paid plus the reductions in this expense sum — if any could be made — would make up the possible source of revenue to the state. No capital stock would be required under state insurance because no dividends would be paid. Whether other savings could be effected will be a topic for later discussion.

It might conceivably be argued that the state would derive a financial gain from assuming insurance, in that a market could be made for its bonds. The insurance business is one which demands long-time investments. The state has such securities for sale. In reply to this argument it may be said that if the normal competitive market price is paid, there would probably be no need to make a market for their securities. If more than the market price is paid, this would again mean the using of insurance for the advantage of some other state activity, and this, it is believed, would not be permitted by the policy-

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holders. But such a use of insurance funds is practically not possible. Only a part of the securities of insurance could thus be invested, because in some states the state securities are not large enough, and second, because they would not fall due at such frequent intervals as would be adequate to pay the constantly maturing policies. There is frequently great concern expressed about the large accumulations of insurance companies. Many imagine it is a concentration of wealth in the control of private individuals to be feared. Many honest-minded men consider these large aggregations of wealth either a proper subject for heavy taxation or a great opportunity for the state to derive profit by directly operating the business. They do not realize that these large sums represent only the small contributions of millions of people, and that the funds are liabilities in the hands of trustees, who should receive no profit from the use of strangers' funds, but only a wage for their services in caring for these funds.

State Insurance may be urged on the ground of its social significance. That is to say, the state will go into the business for social developmental purposes, and not for the sake of revenue. It is undoubtedly this purpose which is commanding

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most attention and which is chiefly responsible for the application of the scheme in the different examples that have been described. The plan appeals very strongly to the social-minded. Many have begun to realize the far-reaching possibilities of insurance as a social institution, and are eager to extend its application by seeking the influence of the state or demanding that it use its coercive power.

It is undoubtedly true that the greatest enemy of life insurance is man's unwillingness to insure. But by what means can this unwillingness be removed? What inducements for insurance can be supplied which are not now present?

Two methods of increasing the number of the insured stand out as prominent, and practically include all others: —

First, by reducing the cost of insurance.

Second, by educating the people to a more general understanding of insurance, and an appreciation of the services which it can render them. If, however, insurance could be reduced in cost, even with the present understanding of it, a great increase in the number of the insured would, without doubt, result.

What, then, is the prospect that under a system

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of state insurance the cost would be reduced and thus the purpose of its assumption by the state would be secured, in that insurance would be extended in its application. This calls for an analysis of insurance costs which cannot give, however, a conclusive answer to the question. For purpose of analysis the costs of insurance may be divided into prime costs and operating costs. The prime costs may be investigated as a cost fixed by the mortality rate and the interest rate, and the operating costs may be divided into the two divisions of costs of securing the business, or the agency costs, and costs of operating the business, or the overhead costs. As to mortality costs little need be said. The state would have no better source of determining its mortality charge than the companies now have, and private companies have, under competitive conditions, quite as much to gain from taking advantage of any improvements in mortality as the state would have. That is to say, if any one company knew it could safely reduce its pure mortality charge, it would usually be quite willing to do so, for the very powerful effect it would have in bringing to it new business by means of a reduction in costs to policyholders. The

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mortality table now in general use in the United States is the American Mortality Table, drawn up in 1869. It was based on a small amount at risk and is redundant, but this redundancy is, to a very large degree, discounted by the select and ultimate or preliminary term methods of writing policies and the dividend-paying practice of the companies. In any case this table is the most accurate which is now available. It is the one which is prescribed for use in the state regulations of ordinary life insurance, and the one which has been adopted in the state insurance plan in Wisconsin. An investigation is now started which will result in a new mortality table, but whatever its showing may be, the policy-holders as a class will not be greatly benefited. It is well to have a new table, for insurance will be made more scientific, but it cannot affect materially the question of private *versus* state insurance. It will simply show to a certain degree the effect of the forces which have tended to improve mortality. The chief of these forces are the more intelligent selection of risks for insurance and the better sanitary conditions of living as a result of advancing knowledge of the problems of health. Nor need much be stated

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in regard to the interest rate as it affects the problem of state and private insurance. The state has no mysterious power by which it can affect the interest rate. The American companies have most of their business on a 3 per cent, $3\frac{1}{2}$ per cent, or 4 per cent interest basis; that is, they assume they will be able to earn such an interest throughout the time of the contract. It is true that most of the companies are earning at present a rate in excess of these rates, but this surplus earning is also either discounted or returned to the policyholder. The average interest rate earned in 1911 was 4.6 per cent. In any event it is not probable that any state would transact the life insurance business on a higher interest basis, nor do the present plans of state insurance assume a higher rate.

It may be argued that a combination of the business of all companies into one business under the state would secure better averages in mortality, and interest. Any one conversant with the theory of insurance knows that the present business of all well-established companies gives ample opportunity for the safe working of the law of average, both as to the mortality rate and the interest rate. It would therefore appear reasonably certain

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that the state would not be able to effect any material saving either from the mortality or interest charges. Hence from these sources it could not reduce the cost of insurance, thereby making it more attractive and salable to greater numbers, which is the particular proposition that is now being considered.

It is possible, as some contend, that under state insurance greater equity as regards classes of the insurable might be secured by minor adjustments of the above charges. That is, a more complete analysis of the mortality experience of different classes and the interest earnings on the policies of these different classes would result in an adjustment of these charges. This result is possible, but it must be understood that this would mean a higher charge for some if it meant a lower charge for others. Insurance cannot be argued as individually just. It does not concern itself with an individual, but with large numbers of individuals. It is a mutual arrangement whose results are always collectively fair and just. The old maxim, "that each tub should stand on its bottom," has no application in insurance. There is nothing, however, to prevent the above adjustments from being made by state regulation under

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a system of private insurance, if they are desirable and possible. The failure to devise a more equitable plan for distributing dividends as regards classes of policyholders and the heavy loading of the net premium on some classes of policies greatly reflect on the scientific character claimed for insurance. The contribution plan of distributing dividends, namely, that each policy should share in the earnings in the proportion that it has contributed to these earnings, is yet far in many cases from actual realization.

Partly as a result of the investigations of the insurance business in 1905 and the succeeding years, and partly as a result of the voluntary acts of some companies, policyholders secured a return of dividends which previously had gone to other persons. Companies can now be but little criticized because they do not return these over-charges to policyholders. Indeed the criticism would be more pertinent to say that an undue return is often made to some classes of policyholders. One of the future improvements in insurance either to be adopted by the companies themselves or forced by the state is a greater degree of equity as regards groups in the returns or dividends to policyholders. Some companies

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are now distributing, in the form of dividends, earnings which could never have been earned by the premium which the policyholder paid who receives the dividends. While it is true that insurance can never be administered as a purely individual matter, yet this limitation or characteristic of it does not excuse the unduly high or low final costs to some groups of policyholders which now exist. Dividends are being paid on first-year premiums which must come from the earnings on old policyholders' premiums.

If the prime costs of mortality and interest do not afford a good prospect of being reduced under a system of state insurance, what prospect of reduction exists in the case of the costs of securing and operating the business? It may be noted at once that it is from these sources that the supporters of state insurance expect to make great savings and hence to make insurance cheaper and therefore more popular. The first part of the question, viz. the costs of securing the business, practically means the cost of having agents to solicit the insurance, and the saving to be effected must result either from doing away with agents or reducing the amounts paid to them. We are not without the benefit of experience on this point.

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Attempts have been made in a number of cases to transact insurance without agents, and the results in each case have not so far justified the policy, so far as extending the social benefits of insurance would be accomplished. One of the best examples of this plan is that of the Equitable Assurance Company of London. This company has been in existence over one hundred and fifty years, and for nearly seventy years its advance has been a retreat. It has about \$25,000,000 assets as a result of its century and a half of existence in the greatest center of population in the world. It has less than two thirds as much insurance in force as any one of several American companies accumulate in one year. Attempts have been made to sell insurance by extensive systems of advertising, but none of these attempts has had such success as would warrant the complete adoption of such a plan for all insurance. Insurance is a service, and not a commodity which can be sold direct from producer to consumer. The people do not yet understand insurance and its benefits. There are a large number deficient either in a proper conception of their duties to themselves and their dependents or in a lack of will power to carry out this duty. Probably not

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10 per cent of the business that is placed upon the books of insurance companies comes by voluntary acts of the insured. The individual must be solicited, either to inform him what his duty is or to persuade him to do his known duty. It is a bold venture to attempt at the present stage of insurance knowledge to sell insurance without solicitors, and few of the state plans of insurance propose it. Very few persons who have had practical experience in the business of insurance indorse such a plan. As greater knowledge of insurance is possessed by the people, the possibility of success of such a plan may be greater. It is sometimes argued that agents would be found unnecessary if all companies would abandon the plan of using agents. This is to say, that competition is alone responsible for the existence of agents. Such a contention implies a belief that people know the benefits of insurance and will avail themselves of these benefits.

It may, however, be urged that a saving may be effected under state insurance by reducing the amounts paid for soliciting the business, if not by doing away with agents entirely. This contention implies that agents are now paid unnecessarily high wages. In 1911 there was paid in salaries,

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commissions, and traveling expenses by the ordinary life insurance companies \$94,277,144. But there is a monopoly neither of supply nor demand to fix price. If agents are highly rewarded, then this opportunity should attract, under the prevailing conditions of free competition, a large number of those who desire to secure this high wage. The insurance companies are always willing and anxious to secure good agents. The opportunity to earn the assumed high wage is present in the great number of the uninsured or the insured who can be persuaded to purchase more insurance. Young men are free to choose the business of soliciting insurance equally among many other employments. Yet there is a dearth of insurance agents. If it be replied, that there are few who are qualified for the work, that is, that a natural monopoly of supply exists, then it must be admitted that those employed earn their wage. Nor is there any reason to suppose that under state insurance the present agents would voluntarily work for a less wage. It is therefore difficult to discover any great saving in costs of securing the business under a system of state insurance, so long as human nature remains as it is and so long as general ignorance prevails regarding the

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benefits of insurance. How rapidly these present conditions will be changed no one can say, and hence the potential economics to be effected in this particular remain unknown.

Insurance officials and agents sometimes justify the existence of agents and the sums paid to them on the ground that the commissions paid represent an investment and a necessary investment, by the old policyholders. Whether this claim can be justified or not depends upon two points. First, has the particular company which the agent represents secured sufficient business to secure the average results from mortality and interest investments? that is, is there sufficient business for the law of average to operate? Second, does an increasing business *per se* bring a decrease in cost? As to the first point, it should be understood that the old policyholder has no interest in having new business secured if he is securing the benefits of the law of average. However much others may benefit from being brought into the company and securing the advantages of insurance, the old policyholder is not concerned except as a philanthropically minded individual. It is true, additions should be made to keep in operation this law of average in mortality and investments, but

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the agency force of most well-established companies are doing much better than this. As to the interest which the old policyholder has in securing new business because it may mean a reduction in cost, that is the following subject for investigation.

There remains, then, this other source from which a saving might be secured under state insurance, viz. the costs of operation. It is from this source that many who favor state insurance think great economies can be secured. In 1911 there was paid for operating or overhead expenses about \$70,000,-000 from an income receipt of \$836,160,804, which is about 8 per cent. The origin of the proposed economies, it is argued, will arise from the fact that in place of many competing companies with numerous administrative officials and clerks, occupying many expensive buildings, there will be one company — the state — with a limited number of officials and occupying but one building. This contention demands careful study, not only as to the general assumption upon which it rests,—viz. that the insurance business is one subject to the law of decreasing cost,—but also as to the extent that savings can be made from specific sources, such as a reduction in rent and salaries for expensive administrators.

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It may be inquired if the insurance business follows the principle, that as the number of items or units are produced — which in insurance means policies sold — the cost per unit decreases. In the following table is given the result of grouping into classes according to the amount of new business written in the year 1911, the one hundred and forty-one leading insurance companies doing business in the United States.

The percentage of the average expenses both to the average new business written and to the average premium receipts is given, but the figures in column (g) are more significant than those in column (f). The value of an average is always limited by the numbers upon which it is based, but it is submitted that the number of companies in each of the classes is sufficient to give a trustworthy basis upon which the different averages are calculated. The high average of the group writing new business under \$1,000,000 is to be explained by the fact that this group is made up largely of new companies which are establishing themselves as going concerns, and consequently the initial expenses are high. This fact also affects somewhat the group writing new business amounting between one and five million. It is significant

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TABLE I

AMOUNT OF NEW BUSINESS WRITTEN (a)	NUMBER OF COMPAN- IES IN CLASS (b)	AVERAGE PREMIUM RECEIPTS (c)	AVERAGE NEW BUSINESS WRITTEN (d)	AVERAGE EXPENSE (e)	PER- CENTAGE OF AVERAGE EXPENSE TO NEW BUSINESS (f)	PER- CENTAGE OF AVERAGE EXPENSE TO PREMIUM RECEIPTS (g)
					Under	[48]
Under 1,000,000	24	86,108	636,666	52,416	7	60
1,000,000 to 5,000,000	50	233,840	2,345,000	125,300	5.3	53
5,000,000 to 10,000,000	27	1,067,185	6,721,037	401,407	5.9	37.5
10,000,000 to 15,000,000	11	2,343,818	13,331,454	711,545	5.3	30
15,000,000 to 25,000,000	12	3,788,666	18,327,166	1,126,583	6.1	29.7
25,000,000 to 50,000,000 (x)	7	9,171,142	35,037,428	2,243,714	6.4	24.4
50,000,000 to 100,000,000 (y)	4	16,973,000	71,790,000	4,082,500	5.7	24
Over 100,000,000	6	64,033,666	194,032,833	14,676,000	7.5	22.9

The values for (x) and (y) combined equal for column (f) 6 per cent and for column (g) 24 per cent.

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that this table shows a decrease in average expenses to average premium receipts as the amount of business written increases. This is not, however, a final proof, as will be noted later, that the insurance business is subject to the principle of decreasing cost, or at least it does not prove that the business can be increased indefinitely with an accompanying decreasing cost. However, an additional and better test of the relation of expense to the increase and amounts of business may be applied, as shown in the following two tables.

In Table II the twenty-three leading companies are taken and grouped according to the increase in their premium receipts during a decade, with a statement of the decrease in the classes of expenses and the total expense. If, then, from this table the average decade decreases in total expense for the given groups are calculated, the following results are given. For the companies increasing their premium receipts less than one million during the decade, 2.52 per cent; for the one to two million group, 4.52 per cent; for the two to three million group, 2.67 per cent; for the three to four million group, 1.83 per cent; for the four to five million group, 7.65 per cent; for the five to six million group, 4.87 per cent; for the six

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TABLE II

COMPANIES	YEARS	GROSS PREMIUM RECEIPTS	PERCENTAGE TO PREMIUM		PERCENTAGE OF TOTAL EXPENSES INCLUDING TAXES TO PREMIUM RECEIPTS
			Of Commissions and Agency Expenses	Of Administrative Expenses	
1 MILLION OR LESS INCREASE IN PREMIUMS					
Berkshire	1910	2,387,150	9.70	5.87	20.38
	1901	2,173,932	12.03	5.75	21.10
Conn. General	1910	1,573,092	14.20	6.57	23.39
	1901	608,275	16.38	9.77	28.39
Manhattan	1910	2,199,371	10.44	12.86	41.34
	1901	2,016,325	19.32	11.20	43.18
Pittsburgh Life & Trust	1910	2,639,542	7.40	8.44	27.13
	1901	2,421,699	21.42	12.67	43.25
Union Mutual	1910	2,220,479	11.45	8.85	24.22
	1901	1,716,298	23.21	12.11	38.57
1 TO 2 MILLION INCREASE					
Conn. Mutual	1910	6,122,457	10.60	5.55	24.52
	1901	5,024,351	8.38	6.62	27.68
Germania	1910	5,284,473	16.26	6.78	25.84
	1901	3,450,115	16.63	7.78	28.31
National Life	1910	5,814,575	13.49	4.83	21.69
	1901	4,133,896	17.35	5.47	27.28
Home	1910	3,588,928	13.22	7.75	24.06
	1901	2,239,523	18.84	9.13	32.42
State Mutual	1910	5,034,779	11.35	5.02	19.55
	1901	3,364,226	14.22	5.94	23.58
2 TO 3 MILLION INCREASE					
Ætna	1910	10,370,013	11.89	5.78	22.44
	1901	7,675,461	12.96	7.59	23.85
Phoenix	1910	4,590,123	14.59	6.50	24.67
	1901	2,523,979	14.67	10.11	28.61

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TABLE II.—Continued

COMPANIES	YEARS	GROSS PREMIUM RECEIPTS	PERCENTAGE TO PREMIUM		PERCENTAGE OF TOTAL EXPENSES INCLUDING TAXES TO PREMIUM RECEIPTS
			Of Commissions and Agency Expenses	Of Administrative Expenses	
3 TO 4 MILLION INCREASE					
Mass. Mutual . . .	1910	8,947,788	11.35	5.49	19.19
	1901	5,133,843	13.68	6.31	22.25
New England Mutual .	1910	7,330,336	12.41	5.11	21.24
	1901	4,231,685	11.31	7.95	23.69
Prov. Life and Trust .	1910	8,448,518	10.62	8.17	21.31
	1901	5,485,068	9.65	4.98	19.19
Travelers	1910	7,107,477	13.60	6.04	21.93
	1901	3,593,938	13.51	6.27	25.54
4 TO 5 MILLION INCREASE					
Equitable	1910	51,027,173	12.87	4.56	20.40
	1901	45,463,740	14.67	6.78	24.45
Mutual	1910	52,106,429	9.23	4.99	17.25
	1901	47,811,869	19.37	6.27	28.50
5 TO 6 MILLION INCREASE					
Union Central . . .	1910	10,424,600	12.45	4.66	22.21
	1901	5,340,670	15.26	9.61	27.08
6 TO 10 MILLION INCREASE					
Mutual Benefit . . .	1910	19,632,149	11.41	5.28	19.48
	1901	10,839,495	10.35	5.40	20.13
Penn Mutual . . .	1910	17,858,958	12.90	4.12	20.46
	1901	8,830,040	15.65	5.93	26.39
OVER 10 MILLION INCREASE					
N. Y. Life	1910	79,547,606	8.83	3.60	14.24
	1901	54,435,814	17.07	6.46	25.35
Northwestern Mutual .	1910	38,743,935	10.79	3.67	17.12
	1901	22,609,544	11.88	4.25	19.73

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to ten million group, 3.29 per cent; and for the over ten million group, 6.85 per cent. If, however, it is objected that a grouping according to increase in premium receipts with reference to the expenses is not a test of the relation of expense to increase in business because of the fact that a small company may show an enormous increase in premium receipts during the decade, while a large company may show a small increase, and because, further, that a particular company may have sold a large number of large premium policies, such as endowments, which would not mean unduly large proportional increase in amount of insurances in force, the following statement may be given of the business of the twenty-one leading companies for the decade 1901-1910.

Six companies had an average business in force for the decade of less than \$100,000,000, and in this group the average decrease in the expenses was 7.35 per cent. Eleven companies had an average business in force between \$100,000,000 and \$500,000,000, and the average decrease in their expense was 3.64 per cent. Four companies had an average business in force of over \$500,000,000, and the average decrease in their expense was 7.25 per cent.

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As reflecting some light on the relation of expense to increased business the following table may be given for the twenty-five leading life insurance companies for the total business of four years.

A study of this table gives some support to the contention that the efficiency of private insurance is increasing. Column (4) indicates that the gross cost for the larger volume of business in 1910 was less than for the smaller volume of 1907, and column (5) indicates that for the same amount expended in 1907 and 1910, almost \$500 more of new business was secured.

Yet none of these tables gives an answer to the question, would the state be able to reduce greatly the expenses of insurance, because it would combine the business of all the companies? Even granting that the tables give some support to the contention that a greater volume of business may be accompanied, and usually is, by a reduction in the expense, it does not follow that the reduction would be a continuous one for unlimited increases in the volume of business. It is in all probability only a question as to how soon forces would begin to operate to cause the business to be done at a greater cost per unit, and it is probable that a

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TABLE III

YEAR	NEW PAID BUSINESS — ORIGINAL POLICIES ONLY	PREMIUM UNIT PER \$100 NEW BUSINESS	GROSS COST PER CENT OF PREMIUM UNIT	NEW BUSINESS SECURED PER \$100 EXPENDED	COMMISSIONS AND AGENCY EXPENSE TO PREMIUM		ADMINISTRATION, CLERICAL AND MEDICAL EXPENSE TO PREMIUM
					54	5.34 %	
1907	\$695,788,800	\$34.90	85.2 %	\$3360	9.54 %	5.34 %	
1908	769,939,000	33.40	80.7	3684	9.59	5.09	
1909	862,929,200	34.80	76.9	3740	10.22	5.20	
1910	956,785,000	35.30	73.7	3812	10.90	4.90	

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state would be no more exempt from the final operation of such forces than is a private company. This limit has certainly not been reached by any of the private companies, and any legislation restricting the amount of new business which a company can write must be justified on grounds other than that it means an increase in unit expense for the business.

As regards such savings in operating expense as salaries of directing officials and other heads of executive departments, there would be considerable opportunity for economy. These administrative positions call for very high-grade ability, but doubtless one medical examiner or one president could direct with efficient subordinates the work of the insurance of the state which is now done by the same officials of the several companies within the state. But this again assumes that these executive officials of private companies are overpaid; that is, that they receive a certain salary for work which does not occupy their full working hours, and that they could be more completely occupied in their field of work.

We need not, at this point, discuss the question whether the state could or would secure and retain men of as high-grade ability to con-

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duct the business as are now employed by the companies.

The savings from rent for most states would not be great, since the insurance now in force in many states has been sold by companies whose home offices are in other states. It is true that some of these foreign companies maintain branch offices, and so far as this is true the possible saving from this source would be augmented. Those states which have old companies with a large volume of business would be able to effect the greatest savings from rent.

It is sometimes argued for a system of state insurance that the policyholder would know definitely what the costs were, and he would not be at the mercy of the companies as he now is. It is said that the prospective purchaser cannot distinguish one company from another as to costs, and that after he becomes a policyholder he has no choice but to continue as a member, however unsatisfactory the returns or costs are to him in his company as compared with those in another company. There is a large element of truth in the statement. He certainly has no choice about continuing a member, unless he chooses to lose his policy by lapsing. Yet it must be remembered

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that a company is not absolutely free to increase costs. A company does not begin nor at any one time has it a complete membership. Continued additions must be made to secure average results in mortality and interest earnings. There is, therefore, the necessity all the time to make a good showing, for there is no greater inducement for prospective buyers than low initial costs. Doubtless many buyers cannot make an intelligent comparison of companies, but the prevailing conditions of competition among the companies prevent unusually high costs on the part of any one company, and the supervision by the state guarantees adequate costs on the part of all. Yet it must be admitted that competition is not so perfect as to secure full protection to the policyholder. For this result to be secured, the buyer would need to have sufficient knowledge to bargain with the seller, and this is not the case with the buyer of insurance. Particular policies are now sold which the purchaser would never buy if he knew more about insurance. Can it be assumed that under the state each kind of policy will be sold at its lowest possible cost, and will have incorporated in the contract every possible privilege for the buyer? Under a state monopoly this comparison could not

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be made. Whether private insurance costs are too high and whether state insurance costs would be lower is the point at issue. However belated some of the reforms in insurance have been, it must be admitted that many of the so-called benefit privileges in the policy have resulted from this competition among companies. This is not to argue that insurance, as now administered, is perfect. Many reforms are awaiting accomplishment. Greater efficiency in many phases of the business can be accomplished. Whether these reforms and this greater efficiency would be accomplished more rapidly under state insurance is a question upon which there is difference of opinion. The officials of private insurance who are interesting themselves in a campaign of public education on insurance should realize what this campaign if it is successful will mean. Demands will be made after the public is informed upon insurance, which will not be easy to meet.

They will demand greater efficiency and lower costs than now prevail. They will demand a better enforcement of the trustee relationship of the officials, and an extension of the insurance principle.

This concludes the consideration of the subject of increasing the number of insured by reducing

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TABLE IV

YEAR	ORDINARY LIFE		INDUSTRIAL		TOTAL
	No. of Policies	Amounts of Policies	No. of Policies	Amounts of Policies	
1870	839,226	2,262,847,000	—	—	839,226
1880	679,690	1,564,183,532	236,674	20,533,469	916,364
1890	1,319,561	3,620,057,439	3,883,529	429,521,128	5,203,090
1900	3,176,051	7,093,152,380	11,219,296	1,468,986,366	14,395,347
1910	6,954,119	13,227,213,168	23,034,463	3,177,047,874	29,988,582

[59]

TABLE V

YEAR	POPULATION	PERCENTAGE INCREASE	WEALTH	PERCENTAGE INCREASE	INSURANCE IN FORCE	PERCENTAGE INCREASE
1870	38,558,371	22.6	\$30,068,518,000	86.7	\$2,262,847,000	—
1880	50,155,783	30.2	43,642,000,000	45.1	1,584,717,001	—
1890	62,947,714	25.5	65,037,091,000	26.1	4,049,578,567	153
1900	75,994,575	21.2	88,517,306,775	20.7	8,562,138,746	111
1910	91,972,266	21.1	107,104,211,917	20.9	16,404,261,042	91

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the cost. There remains the possibility of increasing the number of the insured by increasing under state insurance the knowledge of insurance. This would justify its assumption by the state for social-developmental purposes. In this connection it may be inquired to what extent has private insurance met its opportunity.

Table IV shows increase of insurance by decades.

As a partial but not a conclusive test of private insurance embracing its opportunity, a comparison of the above total of ordinary and industrial insurance may be made with the growth of population and the increase in national wealth. This comparison is shown in table V.

If we consider percentages alone and include the percentage increase in policies as well as amounts of insurance, the following results are shown:—

TABLE VI

YEAR	PERCENTAGE INCREASE IN POPULATION	PERCENTAGE INCREASE IN WEALTH	PERCENTAGE INCREASE IN AMOUNT OF INSURANCE	PERCENTAGE INCREASE IN NUMBER OF POLICIES
1880	30.2	45.1	—	20
1890	25.5	26.1	153	467
1900	21.2	20.7	111	175
1910	21.1	20.9	91	105

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Statistics either as to the number of people insurable or as to the number of different persons insured are not available, and only rough estimates can be made. In 1910 there were in force 38,546,675 ordinary life policies, industrial policies, and fraternal certificates. How many persons does this number represent? Estimates from insurance officials differ somewhat. In one of the oldest and largest ordinary life companies the percentage between the number of policies and different policyholders is 71 per cent. In one of the promising new companies which has been in business six years the same percentage is 97 per cent. However, it must be remembered that while a person may have only one policy in a particular company, yet he may have policies in other companies, and this would result in duplication. Possibly one might venture the estimate that the 7,000,000 policies of ordinary life insurance are held by about 3,000,000 persons, and that the total 38,000,000 policies of all kinds are held by about 20,000,000 of people. These are, however, but estimates in lieu of any definite statistics. However, in order to test the extent to which private insurance has met its opportunity, we should know the number of people insurable, and in this

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connection estimates are more unreliable. A large percentage of the people are insurable in industrial insurance, but a smaller percentage in fraternal and a still smaller number in ordinary life companies. We may use the percentage of the 1900 census and find that the number of males between 21 and 60 years of age is 22,793,946. But women are being solicited for insurance, and children, as well as those over 60, are insurable under the industrial plan. Then, too, by the advances in knowledge, both as to health and from insurance experience, many previously uninsurable are brought in the class of insurable. However far private insurance has failed to insure the insurable, the results which have been achieved, as shown in Tables I and II, acquit the administrators of private insurance of any charge of slothfulness in increasing their business.

It is urged that state insurance would educate the people on the subject of insurance. It is probably true that the novelty of the plan would attract some attention at first, but it is very questionable if any permanent or widespread education would result from the mere fact of state insurance. If the state should enter upon a campaign of public education, this would entail costs which

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would need to be met either from the insurance collections or from some source of state revenue. The greatest single force to-day for educating the people on insurance is the 75,000 insurance agents, and if the state is to transact the business without agents, the campaign of education would need to be planned along very broad lines, and hence the cost would be proportionally high.

Another phase of the educational work of state insurance has been suggested in the effect it would have in stimulating interest in honest and efficient government. Something may be accomplished in this respect; but should a policyholder feel any more interest in the honesty and efficiency of the state official who collected and invested his premium than a taxpayer should feel interest in the honesty and efficiency of the state official who assessed, collected, and spent his tax?

A minor reason assigned for state insurance, as a means of increasing the popularity of insurance, is that the people would have great confidence in its security. Yet it is safe to say that one of the least serious objections to overcome in selling insurance is the one that the companies are not sound. The investigations of 1905 and those made since proved beyond doubt that the financial

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security of the companies is beyond question, and few prospective buyers of insurance offer this as a vital objection to the purchase of insurance.

Again, it is urged that under the state, insurance would be applied to risks not now insured by the ordinary private company. It is pointed out that insurance companies do not solicit insurance from those whose ability to pay premiums is doubtful, although they may be excellent physical risks and might greatly benefit from the use of the insurance principle.

It is well known that the insurance companies endeavor to keep their lapse rate low. Then, too, but few companies will insure other than standard lives; that is, those of normal physical vigor. Could the state afford to insure those of good physical vigor but of limited financial means? Certainly the mere fact of being insured under the state cannot affect their financial ability. That weakness is fundamentally due to other causes. So far as lapses are avoided, simply because they are used as arguments against the company in selling its policies in competition with other companies, so far they could occur under state insurance. But so far as lapses unfavorable affect the cost of insurance, so far the state could not afford

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to have them any more than a private company can. Could substandard lives be insured under state insurance? This question must be answered by deciding whether the state would be more active in collecting data and drawing up tables under which such lives could be insured. It is quite possible that an active and capable department of insurance would make a much wider application of the insurance principle than is now found under private insurance.

State insurance may be urged neither for the purpose of deriving revenue nor for distinctively social purpose, but as the only satisfactory method of regulating a private business. The necessity for such a regulation must arise because of one or more of the following reasons:—

- (a) Because it is or threatens to become a monopoly, characterized by the exercise of oppressive power;
- (b) Because there is unregulated and injurious competition;
- (c) Because the private companies represent unduly large concentrations of wealth;
- (d) Because the policyholders cannot be assured protection by the present system of regulation.

It is sometimes said that insurance tends to

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become a monopoly, and the proof of the statement is given that only a few large companies exist in the several countries, and that these companies make agreements to impose certain conditions upon policyholders. In the United States there are 238 life insurance companies listed in the Year Book for 1911. During the past decade many new companies have been formed. Nor is it true that the companies are either all large or small. Six companies wrote new business during the year amounting to over \$100,000,000 each; four from \$50,000,000 to \$100,000,000; seven from \$25,000,000 to \$50,000,000; twelve from \$15,000,000 to \$25,000,000; eleven from \$10,000,000 to \$15,000,000; twenty-seven from \$5,000,000 to \$10,000,000; fifty from \$1,000,000 to \$5,000,000; and twenty-four under \$1,000,000.

Additional evidence offered as a proof of a monopoly is that the price charged for the service is largely uniform in all companies. This, it is urged, proves agreements among the companies. This evidence cannot be admitted for the reason that insurance costs, at least primary costs, are determined for the companies by the mortality and interest rate, and for the well-known fact that in the United States at least there has been an

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unfortunate lack of agreement among the companies. It has been difficult to secure some co-operation from the companies from which the public might receive great gain. Insurance in the United States has not been injured by agreements, but from the lack of them.

Is there unregulated or injurious competition? It must be admitted that notwithstanding the great improvement in state legislation, enacted for this purpose especially since 1905, full regulation in this respect has not been realized. It is true that the security of the funds of the policy-holders, at least the funds to mature their contracts, is well assured by the state laws regarding the methods of the valuation of policies and the investments of the funds of the companies. But it is also true that new companies are permitted to sell their stocks upon almost any terms in many of the states. Companies are permitted in some states to spend recklessly policyholders' money in building expensive home offices or in other questionable methods of advertising. It is suspected that some companies are permitted to "juggle" their funds in the distribution of dividends, with the result that classes of policy-holders suffer unnecessarily in equitable returns.

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As to the third argument, that private companies represent unduly large concentration of wealth. The large size of a few companies has not been accomplished by amalgamation, as is true with many other examples of "big business" in the United States, but by the development of a single unit. Therefore there has not been for this particular reason a restriction of competition. If, however, the increase in age of the company does not mean an increase in the cost of insurance, but a decrease in cost, or at least a cost as low as other competing companies, is there any good reason to restrict by law the size of companies? We are prone in these latter days to condemn any financial organization that is large, because great evil has been found in connection with some of the large financial concerns. It is, however, probably true that the top of the curve of increased size in the large companies has been reached, for the margin of insurance added each year over insurance lost is growing smaller. But a final answer to the objection is that the states can, as New York now does, restrict the growth of a company by limiting the amount of new business which it may write each year.

Another reason sometimes urged for the com-

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plete regulation of insurance by means of state insurance is that more liberal provisions in policies would be granted. However late some of the rights have been granted to policyholders, there is in the states of most advanced regulation little cause of complaint at present on account of the absence of privileges in the policies. The states have complete power to enforce desirable liberal provisions, and if they do not now choose to do so, it is difficult to understand why they would do this if the states were selling the policies. Such an argument arises from the memory or knowledge of those times when the insurance contract was drawn up with little consideration to the policyholder. Insurance managers have a new conception of their duty to the public, whether this conception has arisen from the compulsory act of the state or has resulted from a new vision of the business.

Such a minor argument, that by state insurance much money would be kept in the state, deserves no critical consideration, were it not for the fact that it is seriously offered by those in responsible positions. It is a modern form of that old argument originated by the medieval mind and still kept alive by those of modern times who afford us

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an example of how this medieval mind worked. Capital is mobile and is not governed in its movement by sentiments of the hearth and home. Capital will remain in the state if it can receive as good return as it can abroad. If it cannot, is there not every reason why policyholders' money should leave the state? for the state must certainly be interested in supplying the insurance — a social benefit — under the lowest possible cost, if the state transacts the business.

Some will oppose state insurance, for fear that it cannot be kept free from the politicians, and not because they do not believe the state should not or could not do this work. It is said that our government is a government of parties, and that the prime object of a political party is to secure control of offices. The evil effects, it is supposed, might result from two sources. First, by a political party in power selecting inefficient administrators of the state insurance. Second, by bidding for votes by promising reduction in costs of the insurance or by the extension of benefits which would impair the security of the contracts, however efficiently the business might be managed. Under our changing party officials it is frequently difficult to realize a high grade of efficiency. Of the 45

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superintendents of insurance in 1902 only 4 were in office eight years later. If this should occur under a system of state insurance, it would doubtless mar the efficiency of the service, if it did not, as it probably would not, prevent the carrying on of the work. Yet it is urged that civil service is an answer to the above objection. But civil service is not synonymous with efficiency. Much depends upon the type of men who direct the civil service and the law itself. For many kinds of ability civil service systems have devised no satisfactory test. Especially would this be true in attempting to test an individual's fitness to conduct a system of state insurance. Civil service has not yet solved the question of what shall be done with the inefficient individual who has secured his position by meeting its tests. The state has not yet succeeded, in the United States at least, in securing and keeping the highest grade of ability. The rewards in private business are often so much greater, especially in financial lines of business and managerial positions, — the important lines in a system of state insurance, — that some provisions would need to be made to meet this demand of private business.

Lamentable as it may seem to some persons,

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the satisfaction which comes from doing a public service efficiently and in doing it for that indefinite, intangible, public good, and the inspiration which comes from being a faithful servant of the people, are not as strong motives to conduct as those which come from the prospect of receiving a full monetary reward for efficiency, and from the pleasure received from winning victories in the competitive game of business. We have many faithful and honest men in public life, but too few efficient ones. It must be recognized, however, that there has been a very great improvement in public service, and that probably even greater improvement is promised. It is becoming the rule to select officials for public service because of their specific training for a work, and not merely by examination. Finally, it may be pointed out in regard to civil service, that it is not chiefly in completely testing fitness for office which promises so much good for the public, but rather in preventing the removal without cause of a public official whose efficiency has been proven by services rendered.

A minor argument offered against state insurance is that there would be an unfavorable selection of risks. If there should be no agents, it is

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said that only those who were much concerned about securing insurance would go to the trouble of seeking it, while other better risks would wait to be solicited by the agents of the private companies. This assumes that there would not be a state monopoly of insurance. Again it is urged, if there were agents who were paid less than agents are now paid, that they would be induced to solicit applications somewhat indiscriminately, in order to secure the many small commissions. The agent of the private company realizes that his position depends upon having a large percentage of his risks accepted by the company. It is also urged that, if there were no agents as such, those state officials empowered to transmit applications would be willing to render the service for any one, and that medical examiners might be less careful than they now are, in that the benefits to an individual and often a friend would be balanced over against the duty to the state. These, however, are gratuitous assumptions which can be verified or disproved only after a longer mortality experience of state-insured risks is available.

It has been shown that only in one case is a monopoly of state insurance provided. This seems very desirable, especially as a plan of pro-

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cedure for the states of the United States. This would give opportunity for organizing the work and making the necessary adjustments in our system of administrating the business of the state and preparing the public for state insurance. It is not probable, however, that even a state monopoly would prevent fraternal or purely mutual insurance, for the state is to assume it chiefly for the social benefits, and if the public is voluntarily doing what the state proposes to urge them to do, there would be no reason to prevent purely mutual insurance.

There remains for consideration but the final question of indemnity to private companies, for it is scarcely to be doubted that the logical result of state life insurance will be the state monopoly of life insurance. This monopoly might be brought about for two reasons.

First, because the state had initiated state insurance and felt that it had properly organized the work, and yet sufficient risks were not being secured.

Second, because it became immediately successful, and the social results were so evidently good, that a complete monopoly would seem quite justifiable.

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In such an event must an indemnity be granted to the private companies? Before inquiring if any provisions of the federal or state constitutions would be a bar to such a monopoly without indemnity, let us consider it from the broader aspect of the relation of a state to its citizens and their property.

In early times it was the fashion to justify acts of the state under the formula that the "state is sovereign and therefore irresponsible," but in the later days of constitutions we are wont to justify acts of the state by other than an appeal to the vague pretext of sovereignty. The question is complicated by the fact that rights of foreigners would be affected by a state monopoly of insurance, since in many states companies of foreign nations have policies on the lives of citizens of the state. Under international law the sovereignty of the state is not positively admitted, and a state is responsible for all violations of the rules of international law, notwithstanding the fact that the act of injury results from a positive national or state law. It cannot evade responsibility by appealing to the sovereignty which authorized the legislative act. But does it follow from this that a state would be responsible for any financial loss

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suffered by a foreign insurance company, if the insurance business was made a monopoly by the state? A recent writer has said on this point that "it is necessary to lay stress on the judicial nature of the act creating the insurance monopoly. The act which creates the monopoly is a law in the full meaning of the word. Law is a general and impersonal rule, and the essential element in a legislative act is the prescribing of a course of social conduct which must be observed by persons in general. The organization of a public monopoly of insurance is essentially for the purpose of regulating the activity of individuals in a certain field." It applies to all, but only to a special field, just as a regulation of commerce, industry, or a profession. It is but prescribing by the legislature that the activity of individuals shall be exercised only in a certain manner and shall conform to a certain idea of social justice and public utility. But it is said that the extent of legislative power will be determined by the character of the thing forbidden to an individual. The doing of certain acts carries with it a generally admitted public injury. Such acts as prohibiting the importation of immoral books, the manufacture and sale of harmful drugs, are too well established to need a discussion of

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their justification. All such laws depend upon the ideals of justice prevailing at a given time in a country which requires the state to protect the physical and moral welfare of its citizens.

But a distinction is to be made in regard to a state monopoly of insurance. In such a case, not only is the individual to be denied the right to engage in the business, but he is to be forced to give up his property rights in the business, and the state is then to do what it prohibits the individual from doing. It may be urged that every legislative reform is a gain for some and a loss for others; that progress would be impossible if, at each stage of its forward march, it were necessary to pay toll to the privileged ones who were profiting by the preceding circumstances. But does the state enrich itself? It has no wealth other than that of its citizens. The state assumes the monopoly for the social benefits resulting, and not as a source of revenue. A damage which can secure an indemnity must secure it from the fact that the damage was a special one. For the welfare of the community the monopoly of insurance is assumed. A damage is caused to those who were in that business, but it is a loss borne for the common interest, and no particular individual benefits from the

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damage inflicted. The damage done by a law of this character is never a special damage because the general impersonal character of the law itself is contrary to it. It cannot be said that those engaged in the business at the time of the enforcing of a state monopoly of insurance would alone suffer a loss. Every one who intended to engage in the forbidden industry might be said to suffer a loss, and an acceptable doctrine of special damages might be held to include this class. Nor can it be held that the damage arises from any damage to tangible property, since an insurance company has but little of real property. It is the taking away of an employment and the prospective income which results from labor. It must be granted, however, that, waiving any general question of the rights of the individual and the duties of the state, there are specific provisions in our federal and in our state institutions which affect the monopolization of insurance by the state.

The fifth and fourteenth amendments forbid the depriving of any person of property without due process of law. The fifth amendment states further that private property cannot be taken for public use without just compensation, and the fourteenth amendment forbids any state to deny

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to any person within its jurisdiction the equal protection of the laws. Again, the federal Constitution forbids the impairment of the obligation of contracts, and provides that citizens of each state shall be entitled to all the privileges and immunities of citizens in the several states. What troublesome questions might arise under these provisions or other provisions of the federal Constitution in the event that a state should endeavor to monopolize insurance cannot be predicted.

The insurance policies are contracts made between the company and the citizens of the several states. They are contracts extending over long periods, and by their number and character establish a certain species of income yielding property for the officials of the company, at least in the case of stock insurance companies. What other questions would arise from the provisions of the respective state constitutions only an examination of state constitutions would disclose. However, all these difficulties need not probably prevent the state from monopolizing the insurance business. For the reason that insurance companies existing at the time of monopolization would suffer a pecuniary damage, and for the fact that these constitutions do present difficulties, the better way

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would probably be to grant the companies the right to maintain their existing insurance, but to prevent them, after a certain period, from writing new policies. This would give the state an opportunity to organize its work and the companies an opportunity to adjust their business.

II

FIRE INSURANCE

CHAPTER IV

THE NATURE OF FIRE INSURANCE

IT is necessary to inquire into the nature of fire insurance, and especially to make a comparison of it with life insurance before the discussion can proceed to the next topic of investigation, viz. is the business of fire insurance one suited to transaction by the state?

Many mistakes in the regulation of insurance have been made by assuming a similarity in the character of the various kinds of insurance when no such resemblance exists.

The fire insurance contract is a personal contract of indemnity. Its personal character is not peculiar to it as a contract, since most insurance contracts are of this description, but the personal factor is to be emphasized somewhat more fully in the fire insurance contract, since the one party to the contract — the insurer — is, under the present methods of conducting the business, very dependent upon the utmost good faith being shown

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by the other party — the insured. In life insurance the medical examination can be made searching and almost all undesirable risks be excluded, and therefore the chances of immediate and heavy losses be avoided. But in fire insurance the most rigid inspection of a building can only tell the company what its probable construction and exposure hazards are, leaving yet largely unknown the important hazard of continued occupancy and the moral hazard. Daily inspection cannot be made by the company to discover the manner in which the insured uses his building, his carefulness, and his honesty in making the contract.

The fire insurance contract is also one of indemnity; that is to state, it is one by which the owner should receive a sum equal to or at least not in excess of the value of the property destroyed. It may indeed be less, because the insured has chosen to purchase only partial indemnity, but it can never, except in case of personal dishonesty or ignorantly enacted state laws, be more than the value of the property destroyed. In life insurance no such indemnity is implied in the contract, for the very good reason that life is an immaterial thing which lends itself only to very rude calculations of its money value.

NATURE OF FIRE INSURANCE

The value of real estate, and especially personal property, is continually changing. The latter class of property is suffering depreciation, either by use or the continual changes in market conditions of supply and demand. Therefore even the value of the property expressed in the contract at the time of writing the policy should not be accepted as final in determining the indemnity when the loss occurs, notwithstanding that it may seem to the insured that he purchased so many thousand dollars worth of protection at the time of forming the contract. The indemnity should be based upon the actual loss suffered, else there will be an inducement offered to buy insurance for the purpose of a gain, an idea repugnant to the essential principles upon which all insurance is based. But no such question arises in life insurance. The insured purchases the right for his beneficiary or for himself to receive a certain stated sum of money at death or after a stated interval of time. No considerations need be given as to what the individual's life is worth. He cannot possibly gain from this contract, at least in the sense in which gain from an investment is used. It is true that fire and life insurance resemble each other in that the underlying principle of coöpera-

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tion is the same. This is true in all kinds of real insurance. This is but to state that insurance is a method of associating groups of individuals exposed to a risk whereby a certain degree of certainty is secured in place of total uncertainty. The groups, by assuming what was formerly an individual burden, reduce this burden for each. Indeed in fire insurance this coöperation of the insured group reduces the burden for the uninsured in that fire insurance, by requiring or at least encouraging better methods of construction, better protection to property, and more careful use of property, reduces the risk of those uninsured. The mere fact that the loss by fire in the United States is not being annually reduced is no proof, as some contend, that fire insurance does not tend to reduce the fire loss. Such a view is only slightly more superficial than the related one, that fire insurance is a tax. A tax is a compulsory charge, collected by the state upon all property with certain well-known exceptions. But the fire insurance charge is not borne by all property holders. It is not compulsory. Nor is it wholly true that the companies selling fire insurance simply determine the loss by fire and pro-rate it among classes of property holders. They

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are not indifferent as to losses by fire, nor can the loss be prorated with the nicety possible in the case of a tax. Classes of property show at different times and in different regions great variations in the loss ratio, and all classes of property at the time of a great conflagration show abnormal losses.

There arises therefore the question of relative risk in fire and life insurance. It has been shown that the chief elements of the risk in life insurance are found in the mortality rate and the investment rate. The burning rate corresponds, so far as there is any correspondence, to the mortality rate in life insurance. There is, however, greater homogeneity among insured lives than among insured properties. In life insurance a selection of normal lives has been made, and while these lives lend themselves to certain classifications on the basis of sex and age, and while experience of such insured groups shows certain marked variations from the assumed rate of mortality, yet there is this original selection of normal lives which insures a large degree of homogeneity in the group. Because the original basis had a large degree of uniformity in it, a safe degree of uniformity is assured in the result or experience on such lives. The risk is not, therefore, from the standpoint of

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the insurer, great, so far as the mortality rate is concerned.

In fire insurance there are many kinds of property, differing not only as to construction, but also to the use to which it is put and the care with which it is used as well as to the extent of danger of its loss by adjoining properties. Heterogeneity rather than homogeneity is the characteristic. It is true that a certain selection is made as in life insurance, but it is not a selection which secures an equal degree of uniformity. A frame drug store in an outlying district may be quite as good a risk as a brick drug store in a congested district. There is not, therefore, possible that selection of buildings of the same class and description which is possible in life insurance by the medical examination.

A particular class of buildings, as, for example, dwelling houses, may even show a favorable return for one year in one region and an unfavorable result in another region, or the class as a whole may show good results for one year and poor results for the next year, due to a heavy loss in one place. There are also forces in operation which tend to produce decided changes in comparatively brief periods of time. The use of new

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building materials, the enactment of more stringent building codes, and the improvement in fire protection are but examples of the causes which very materially and quickly affect loss ratios on different classes of buildings and in different regions.

However great may have been the advances in medical science and the discoveries in hygiene and sanitation, the effect on insured lives will show itself slowly. It is sometimes stated that fire insurance differs from life insurance in that the former has a rate for each risk, while the latter makes rates for classes of individual risks on the basis of their age and general physical vigor. This is true to a certain extent, as will be shown later in detail, but the comparison can easily be pushed too far. Schedule rating with its specific charges for specific features of the risk has done much to individualize fire insurance rates, but there is a very definite and desirable limit to the individualizing of fire rates. What is needed most is not great individual justice in rates, but greater equity in the rates upon classes of property.

But a more important aspect in the question of the relative risk of unexpected loss in fire and life insurance arises in connection with the adequacy

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of rates as a whole rather than with rates on particular classes of property. Is there any danger that the collections made will not be sufficient to meet losses? Would the state in conducting the business of fire insurance have unexpected burdens placed upon it? Thus arises the problem of conflagrations. It is a well-known fact that this country has experienced these enormously large losses by fire at different times. They are a risk which it seems necessary to provide against at least for many years in this country. Statistics show that there have been since 1900 eighty-one fires in the United States in which the loss was over \$1,000,000. The total loss of property in these fires was \$561,375,000, or an annual average of \$6,930,555. This includes only the large fires. The annual fire loss is, of course, considerably greater. In no year since 1883 has it been less than \$100,000,000, and during the past thirty-seven years, 1875-1911, it has aggregated \$5,337,-215,795. Owing chiefly to these conflagrations, the capital in fire insurance has been replaced over three times since 1871. It was said that the San Francisco fire destroyed the profits of fire insurance in the United States for the past seventy years. When these large losses of property occur,

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money must be immediately paid out from some source to replace the destroyed property. If the state is conducting the fire insurance business, whether in competition with private companies or as a monopoly, this fact will demand large and immediate payments by it to those who have suffered the loss. Thus will be introduced a problem of financing for the state. It must either have been accumulating a large surplus from the past premiums collected, or it must, by the sale of bonds, secure ready money to pay the losses. In the former case the state would have been charging such rates in excess of current losses as would accumulate this conflagration surplus, and this accumulated surplus would supposedly be carried as a deposit in financial institutions. In the case of a proposed sale of bonds, great difficulty and probably impossibility would arise. The effect of attempting to market by any one state sufficient bonds to pay the losses of a San Francisco or Baltimore fire would be disastrous, even if there were not, as there now are in practically all states, certain restrictions upon the issue of state bonds. Certain formalities, if not consent of the legislative body, would be necessary, and yet the fire losses should be paid as quickly as possible.

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There is nothing in life insurance to correspond to the conflagration in fire insurance. To argue that plagues establish this correspondence is as absurd as to argue that conflagrations are unnecessary. They may not be necessary, but they are inevitable so long as our present methods of construction, fire protection, and legal theory of liability for loss are continued.

The risk in fire insurance is therefore quite differently affected by the burning rate than the risk in life insurance is affected by the mortality rate. The burning rate is a more complex factor; it is made up of many incongruous elements which but very remotely correspond to the causes of death. It is true that there is what is called an average annual fire loss, but it is quite a different average from the average death loss. The former is made up of many fluctuating factors. The latter is comparatively stable over long periods of time.

The second element affecting the risk in fire insurance is the investment risk. This corresponds more closely to the investment risk in life insurance, in so far as in both cases advance payments are made for a possible loss, and these advance collections must be kept securely and advantageously invested. The problems arising

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in connection with the investment of the funds in both cases are much the same, and the risk element should not in general be greatly different. There are, however, points of dissimilarity in the financial aspects of life and property insurance. The contracts in fire insurance are for much shorter periods of time than in life insurance. They usually run from one to five years, and this means that the general fund is made up of many more elements which are continually changing.

In the case of life insurance the assets, with the exception of a nominal capital stock, are the property of the policyholders, and the officials, whether of a stock or a mutual company, are very largely in the position of trustees of the funds. But in fire insurance a larger part of the fund does not belong to the policyholders. From one point of view it is only the unearned premium reserve which belongs to the policyholder, and any policyholder's interest in this reserve ends at the close of his contract; that is, at the end of one to five years. It is true that fire insurance companies accumulate a surplus to pay unexpected losses, as in the case of a conflagration, but to argue that a policyholder at a particular time owns a part of this surplus which may be used ten years later

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to pay a conflagration loss when this policyholder is no longer a policyholder is stating an argument supported neither in law nor morals.

The officials of a life insurance company are expected to invest the funds of the company so securely and so safely that the owners of the fund may not only be assured that their policies will be paid when they mature, but also that they may receive either dividends on participating policies or low initial costs on non-participating policies. Indeed the sum total of life insurance assets is not presumed to be divided at any one time among the then living policyholders, and the investment of these funds so that good returns are secured is very important. But the policyholder in a fire insurance company can have no great concern regarding the earnings upon the investments of the company. He does not expect a dividend unless perchance he is a member of a mutual company. But these companies do but a small part of the fire insurance business at the present time. He is chiefly interested in knowing that his loss, if it occurs, will be paid by the company. Whether this payment comes from the premiums collected either with small or large earnings upon them is a matter for the officials of the company and the

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state and not for him. It is true that competition among companies and the laws of the state do assure certain earnings for these funds, but the policyholder in fire insurance has neither the same right to nor interest in the earnings on fire insurance assets as in life insurance assets.

The business of fire insurance is conducted by both mutual and stock companies. In 1911 there were 325 domestic and foreign stock companies doing business in the United States and 268 mutual companies. The net premiums collected during the year by the former were \$225,795,533, and by the latter \$36,618,986. The total disbursements of the stock companies were \$306,799,-882 and of mutual companies \$137,418,230.

The business like life insurance is subject to the regulation of the states, with the result that great variation in the method of regulating the business has resulted. Probably the conflict in state legislation is greater in the case of fire insurance than in life insurance. Fire insurance like life insurance is essentially mutual in its character, but the degree to which mutuality can be applied in its actual transaction is limited both by practical considerations and theoretical justification. The principle of mutuality always implies likeness, and

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it has been shown that differences are more characteristic of property for insurance purposes than difference among individuals for life insurance. In the one case the dissimilarity is a physical fact entering into the risk. In the other case essential dissimilarity has been eliminated by the medical selection, and whatever differences remain do not materially affect the risk.

The mutual principle in fire insurance should be limited therefore to classes of property which have a fair degree of likeness in order to avoid inequity in costs. If, for example, the owners of farm property and of manufacturing property should ally themselves in a mutual fire insurance association, the differences in the character of the property, the use to which it is placed, and the protection about it from fire would almost certainly assure that one group would be bearing the burdens belonging to another. Insurance is one of the costs of production, and the consumers of a particular commodity should expect to pay all the costs of its production rather than to permit its insurance cost being assessed on other commodities. The consumer of bread should not be asked to pay a part of the costs of producing patent medicines.

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It was thought at one time by many insurance officials and agents that classification furnished the real solution of the problem of rating. Many people who are not versed in insurance matters yet believe that rates can be based wholly on the classification of losses on different kinds of property and business. Experience has, however, proven that classification in itself affords no solution to the problem, for its use is limited. It is desirable to have the tabulation of losses on different classes of property; as, for example, dwelling houses, sprinklered risks, and mercantile risks, and even on classes of property within these general classes. However, it is only the general classification which is of great significance in determining what rates are adequate and equitable.

In retail or wholesale mercantile risks there are a great variety of concerns; as, for example, retail grocery stores, hardware stores, drug stores, and likewise a great variety of wholesale establishments. If it were attempted to make a rate for each of these detailed classes, interminable difficulty would be experienced without any promise of equitable or fair rates for the purchaser of insurance. The scientific schedules, such as the Dean or Mercantile Schedule, do not attempt to

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make a rate for each class of the above description, but rather to supply a method of assessing the proper charge for each element in the hazard. That is to state, these schedules rightly assume that a defective flue in a grocery store is quite as significant for the rater in producing a fire loss as an equally defective flue in a drug store; that a rubber hose connection for a gas fire is quite as dangerous in a wholesale dry-goods establishment as in a wholesale drug house. In other words, scientific rating seeks to appraise the hazard of the component parts of a risk and assess the cost upon each. It does not attempt to classify risks endlessly and make a flat charge upon each on the basis of the experienced loss. The theory underlying the method of establishing the cost of indemnity, when a schedule system of rating is used, has been well explained by A. F. Dean, the author of the Dean Schedule. "Under the theories of the Analytic Schedule,—the Dean Schedule-rating is not called rating, because as a system it does not directly seek to establish the selling price of the fire indemnity, but through analysis and classification to establish the amount of hazard in each risk as compared with other risks. The analyzed parts of a hazard are the bricks that build

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up the total hazard of each risk, and as bricks may be used to build any building, so the parts in the schedule may build up the estimate of any risk. We cannot assume that risks themselves are amenable to the law of average without assuming that each of the parts are equally amenable to average. If each part has its own average, this average must stand in a permanent quantitative relation to all the other parts. The synthesis of parts that establishes the quantity of hazard in a risk, establishes at the same time the same permanent quantitative relation between the hazard of this risk, as compared with all other risks, similarly measured, that exists among the parts themselves. It matters not what trade name a risk bears; for if its hazard has been measured by the same scale of measurement, it stands in a position of permanent relativity to other risks, regardless of what we may call them. Of the four main divisions of fire hazard — protection, structure, exposure and occupancy — the last and only the last makes the hazard of one property class differ from another. The containing building may or may not be under municipal protection; it may be of any dimensions or character of material, and it may be unexposed or so exposed that exposure

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constitutes the greater part of its total hazard. The basis rate which stands for unanalyzed hazard does not in theory embody any of the hazard of occupancy because it serves as the basis upon which the charge for occupancy is superimposed."

CHAPTER V

SHOULD THE STATE MONOPOLIZE FIRE INSURANCE?

AFTER this general characterization of fire insurance it may now be inquired if it is a business suitable for state activity. The inquiry may be pursued again on the ground of the purpose of the assumption of fire insurance by the state. Should the state assume it for financial reasons, or as a means of securing satisfactory regulation, or for the social value resulting?

First, then, what would be the justification for the state to use the fire insurance business as a source of revenue? This calls for an investigation of the profits which stock fire insurance companies make, since purely mutual companies return all excess collections to their policyholders. In 1911 there were 325 stock fire insurance companies doing business in the United States, with a capital of \$97,703,288. Their net surplus was \$217,307,406. The dividends paid were \$12,637,-272, or 13.9 per cent if calculated for the year on

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the capital stock, a result which gives an erroneous idea of the actual earnings in the fire insurance business, as will be shown later. The above sums are impressive and would seem to supply a large and promising source of revenue for the state treasury.

Every stock fire insurance company has two distinct sources of income. First, the earnings from its invested funds, and second, the profits, if any, from the sale of its policies. With the first source of income our investigation is not concerned, since it promises no source of revenue for the state. There is no reason to suppose that the state would be able to secure a better interest return than is now secured by the companies. There would, of course, be no capital stock under state fire insurance. It may be urged that the state could use the funds collected as premiums to finance the state; that is to say, since the collections would be in excess of current losses, the state might receive the interest on this excess. Doubtless this contention is true, but such a gain can scarcely be called a profit or a legitimate source of revenue for the state. It is similar to the earnings on the cash in hand collected by taxation in excess of current state needs. This balance does

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produce some revenue, but the insurance receipts or whatever balance on them was held could not be held in the form of cash on hand. The state would be forced to invest these funds in securities just as the companies now do. The state would receive interest on the surplus held for the purpose of meeting losses, especially conflagration losses, since these would be invested. But a limitation on the character of this investment might cause embarrassment. These funds must necessarily be invested in rapidly convertible cash securities, since the demand for these funds in the case of a conflagration would be immediate and large. It is not in this respect that the state would find sufficient warrant for taking over fire insurance for the purely financial advantages. Such a gain for the state would be trivial. There is, however, this second source of revenue, namely, the profits which now go to private insurance companies from the sale of their policies, that is, the underwriting profit.

The total premiums received each year, less expenses and payments made for fire losses, constitute this profit on underwriting, and if such a profit exists, a possible source of revenue for the state exists, assuming that the patrons of state

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fire insurance would be willing to pay in premiums such an excess and not insist that they purchase their indemnity at cost.

Statistics show for recent ten-year periods that the average loss is about 60 per cent of the total premiums and the average expense is about 38 per cent of the total premiums. The 38 per cent is divided into approximately 21 per cent for agents' commissions and 17 per cent for salaries, rents, and other operating expense. It will be observed that underwriting cost hovers very closely about total premium collections. In some years it exceeds them, and in some companies it exceeds them for a number of years. Yet it has been stated that the dividends of stock fire insurance companies of 1911 averaged 13.9 per cent. Herein lies a paradox which has led to confusion in the minds of legislators and prospective investors in fire insurance stocks. The percentages named in the reports of companies as dividends earned are based upon the capital stock and not on the indemnity sold. There is a wide disparity between the capital stock on which dividends are declared and the actual assets which earn these dividends. For example, a company may have been organized thirty years ago with a capital

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of \$200,000 and now have net assets of \$2,000,000. Many companies do not increase their capital stock, but permit whatever underwriting profit there is to accumulate as a surplus. They pay their annual dividends from the earnings on their invested assets. The above company might declare, for example, a dividend of 100 per cent, but this would be 100 per cent on their capital of \$200,000, which would be but 10 per cent on their invested assets.

The statistics of the National Board of Fire Underwriters show that for the decade ending Jan. 1, 1900, the average underwriting profit was about one third of a cent out of each dollar of premiums received, and the same official statistics for the years 1898–1910 show the following facts. Of 114 companies which received premiums during the decade to the amount of \$2,346,877,609 there was paid out as losses and underwriting expenses \$2,390,945,059, or a ratio of losses and expenses to premiums income of 101.8 per cent. Of the one hundred leading companies operating in 1910 seventy-seven made an underwriting profit and twenty-three a loss.

This, however, proves neither that fire insurance is transacted at a loss nor that there would be no

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source of revenue for the state, if it should assume the business. The above figures do not include the earnings from the investments of past premiums upon which there had been a profit and which are now held as a surplus; nor do they include the earnings on the capital stock, although the earnings on the capital stock should not be considered in determining the question of profitability of the fire insurance business for the state. This is true because the stock-holders might withdraw their capital and invest it in other enterprises and secure the normal return on capital, and the state would not, in case it assumed the business, have any capital stock to draw an interest. Again, the statistics include the large sums expended as expense, and it might be that this expense could be reduced under the state's conduct of the business. The figures do show, however, that as the business is now conducted fire indemnity is sold practically at cost; that is to say, the average annual premium receipts for a series of years do not usually exceed by a very large sum the average annual liabilities, due to the fire loss and the expense of conducting the business. The expenses of fire insurance have some peculiar characteristics. In the first place,

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it is an expense for the production of a service, the total expense of which cannot be known at the time of the sale. In the production of most commodities the total expense for their production is fairly definitely known in advance, and the price of the commodity bears in general a very definite relation to the total expenses of production. But in fire insurance the seller of the indemnity does not know at the time of sale what it will finally cost him to pay the indemnity. The future alone can disclose how much property will be burned. For example, a certain company paid out last year \$94 out of each \$100 collected in premiums on a certain class of risks which were written on a three-year contract. There remains \$6 out of which to pay the losses of the remaining two years of the contract. This is not an especially exceptional case nor is it a company which carelessly writes business. In the second place, fire insurance is conducted as a retail business, and therefore it is subject to all the numerous expenses of a middleman business. From the local agent to the general agent, to a department, and then to the home office is a long road with many toll takers. In the third place, the expense element is affected by so great a number of changing factors

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that the past serves as a very imperfect guide for the future.

A brief analysis of fire insurance expenses may be given with a view of discovering the possible sources of reduction. At the close of 1911 the companies reporting to the New York Department of Insurance showed a total expense item of \$116,900,483. Of this total \$24,140,938 was paid for salaries and wages for home office employees. This was approximately an expenditure of 4.4 per cent on their \$535,000,000 assets and .0058 per cent on the \$40,000,000,000 value of the property insured. The losses on investments and securities sold during the year were \$788,343, and for other expenses, excluding commissions, the sum of \$27,125,528 was paid. These expenses include many items, such as rent, advertising, traveling expenses, and taxes. Deducting the above sums from the total expenses of \$116,900,483, there remains \$64,842,912 which was paid for commissions. It is possible that some saving might be effected from a number of the minor items of expenses, such as advertising, rents, etc., but since no one of these in the aggregate is a very large item, the saving on them as a whole could not very materially affect the cost of insurances.

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The three large items in the expense are: (a) for salaries, (b) for taxes, and (c) for commissions. It is not believed that the officials of fire insurance companies as a class are overpaid. There are doubtless examples as in any other class of business where the officials of the company are paid an unduly high salary, but there are no monopolistic conditions from which fire insurance officials as a class are able to benefit.

As to taxes, there is a possibility of great saving. The report shows that the fire insurance companies paid in 1911 over \$8,000,000 as taxes and license fees. If this were reduced to the proportion which fire insurance companies should pay to maintain efficient insurance departments in the states, a very considerable saving could be accomplished. There is, however, no immediate prospect that taxes will be reduced. Insurance companies afford to legislatures in these days of increasing state and local expenditures an easy and available source of revenue, criteria for taxation which have always appealed to the legislator, regardless of the essential justice of the tax.

It is probably the third item, the commissions, which will appeal to many as the largest possible source of saving. This \$64,842,912 for commis-

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sion represents somewhat over 12 per cent of the assets of the companies and 22.05 per cent on the average premium receipt. The Year Book of the Spectator Company shows that the average commission in 1860 was about 11 per cent, in 1890 about 18 per cent, and in 1900 about 20 per cent. The difference in the average commission paid in 1900 and the present is therefore less than 3 per cent. The statistics of the United States Bureau of Labor show that the retail price of food increased 16.1 per cent between the years 1899 and 1906. This translated into the language of the market means that the dollar of the fire insurance agent now buys him much less of consumable commodities.

The chief criticism on commissions is not, however, that commissions as a whole are too high, but that for certain agents and for certain classes of risks unnecessary amounts are paid. Mr. S. R. Barton, State Auditor of Nebraska, in a recent address shows that over \$9,000,000 would have been saved during the year 1911 if the graded commission plan of the Western Union had been observed. It is urged that preferred risks are often a source of unnecessarily high commissions as well as a source of discrimination. It has also been sug-

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gested that agents' commissions be paid only on that portion of the premium represented by a rate of 1 per cent or less.

It has been suggested that a general limitation be placed on expense. If a law should be passed, limiting the amount which could be expended to some fixed ratio, as, for example, 35 or 40 per cent, the effect would be to retire a number of companies and to place a great strain upon a number of other companies. However, such a law might achieve a very desired end for the buyer of insurance, especially if a carefully devised law for regulating rates was enacted.

If the question of a state monopoly of fire insurance is considered strictly on the basis of its possibilities of yielding a revenue to the state, yet another question must be investigated. This is the subject of taxation. If financial considerations alone govern, the state must realize that it will lose the revenue now secured by taxation. This is not an inconsiderable sum, as is shown by the amount of taxes paid by the one hundred and eighty companies reporting to the New York Insurance Department. This amount in 1911 aggregated \$8,236,529. Viewed as a financial problem alone, the state would need to make econ-

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omies in the expense of conducting the business, which would at least be equal to the taxes received in order to avoid a financial loss. It is true that the state would receive, as the private companies now do, an interest return on whatever surplus it would build up, but it must be understood that a surplus in the case of state fire insurance would arise only from excess annual charges for fire indemnity. There would be no capital stock. What the capital stock of private companies now earn is of no public concern, unless, perchance, it be unduly high. The stockholders might withdraw their capital in fire insurance and secure the normal return in other investments.

It must be recognized that certain elements in the expenses of fire insurance as contrasted with life insurance are of a more permanent character whether the business be conducted by private companies or by the state. Advances in knowledge concerning insurance and the benefits which it has may reduce the cost of persuading people to buy both life and fire insurance. But in fire insurance the inspection work connected with securing a risk and retaining it is quite different from the medical examination. A large corps of inspectors will be necessary in fire insurance,

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not only to examine thoroughly the risk when it is written, but also to examine it from time to time, either when the policy is renewed or to see that proper care is exercised in the use of the property. Indeed no other weakness in the fire business at present is more productive of evil and inequitable results than this absence of adequate inspection. Much more should be spent in inspection work than is now the case. No other one thing would tend so forcefully to reduce the useless fire waste. Companies complain that this would largely increase the expense, but it is quite probable that in time the costs of fire protection would decrease. If companies would more readily cancel policies when the hazard of occupancy unduly and unnecessarily increased on account of careless use of the property, and refused to accept risks until a careful inspection had been made, losses heavy in the aggregate would be avoided, and hence the rate would be favorably affected. This practice would enforce more careful building and more careful use of property. The excuse offered by the companies is that competition forces them to follow the old policy. It is an expensive kind of competition for which the consumer — the property owner — is paying a high price.

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A second purpose of the state entering the business might be for the purpose of complete regulation. This would necessarily involve a state monopoly, and the justification of the assumption must be decided on the basis of the necessity for regulation. The particular reasons for the regulation of the business by a state monopoly would again be, as in the case of life insurance: (a) is monopoly threatened under private ownership? (b) is the competition, if it exists, of a kind by which the public is injured by unnecessarily high or inequitable charges? (c) is the business of a peculiar character which makes regulation difficult and unsuccessful?

Monopoly would be indicated most clearly either by a consolidation of previously competing organizations and failure of new competing companies to be organized or by the evidence of agreements as to charges by ostensibly competing organizations. The Fire Insurance Year Book shows that there were 325 stock companies and 268 mutual companies operating in the United States at the close of 1911, and statistics since 1860 show further that the average number of companies for each decade has tended to increase. It is a well-known fact that new fire insurance

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companies are frequently organized, although only a small per cent of the new companies, especially the new stock companies, ever prove a success. At the close of 1911 there were 148 fire and fire-marine insurance companies in the hands of receivers. Practically all the large and markedly successful fire insurance companies, whether stock or mutual, but especially the former, are companies which have been in business for more than a decade. These facts might seem to be presumptive evidence of the existence of some kind of monopolistic power, but such is not the case. At least there is no artificial monopoly power to prevent the organization and operation of fire insurance companies.

There are, however, very great obstacles in the very character of the business which make the chance of new companies succeeding much less than for new organizations in most industrial fields. This is not because there is any real surplus of fire indemnity for sale in respect to the demand. In the large centers of population there is, in general, a dearth of indemnity for sale. This is due to the fact that many companies do not write risks in the congested districts and all companies limit the amount of property which they

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will insure in such districts. Then again there is much property upon which either no insurance or an inadequate amount of insurance is carried. In 1911 the one hundred and eight leading fire insurance companies had outstanding policies which covered \$46,276,992,650 of property, but this does not represent the market value of all insurable property in the United States.

Nor are the legal requirements regarding the formation of a company difficult to meet. Yet the net book as well as the market value of practically every one of the one hundred and seventy-five fire insurance companies is well over the par value of the stock. This last fact is to be explained by the usually common practice of selling the stock of a fire insurance company at a premium in order to lay the foundations of that surplus which is essential to the success of every fire insurance company.

It is also in connection with this surplus that the chief explanation of the frequent failure of new companies is to be found. The new company has the heavy initial expense of organization; of selling its stock; of securing an agency force. It must then go into the field and compete with the old-established companies to secure business.

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It may find it a difficult matter to secure the better class of risks. It may endeavor to secure them by cutting rates, but the old established company can afford to meet this competitive rate. It may offer the inducement to the agent who probably represents both companies of a commission which will secure the business for it. The old company is a going concern and is presumed to be efficient, having already secured sufficient business to bring whatever economies there are from large scale operation. If the new company does secure the good risk, it may have been forced to make such concessions that a favorable return on the risk will not be secured. If it is forced to accept the poor risk, it is likewise in an unfavorable position to secure a good return. Yet it must secure business on such rates that a surplus can be gradually accumulated for that time which is almost certain to come to every fire insurance company when the losses are heavy. This may be caused by a heavy loss on several large risks in several localities or it may be caused by a destructive fire in a particular locality.

The report of the Superintendent of Insurance for New York in 1911 shows that from the time of the establishment of the department in 1859 until

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the close of the above year 188 stock and mutual fire insurance companies had gone out of business. Of the 105 companies reporting to that department in 1871 only 19 were in business in 1902. Forty-six of the companies organized since 1871 had retired by 1911. In short, more than three fourths of all the companies in business in 1871 had retired within the next twenty years and two thirds of all those organized since 1871 had retired within the next twenty years. Yet new companies are continually being formed, and at the close of 1911 there were in that state 162 fire insurance companies reporting to the state department of insurance.

The facts, therefore, do not show that a monopoly exists either from a consolidation of existing companies or from a failure of new companies to be organized. Whatever limitations exist in the latter particular result from the natural obstacles to the establishment of a successful fire insurance company and not in any artificially established restrictions.

But the evil of a monopoly may occur if ostensibly competing organizations have agreements as to the charges which will be exacted from the consumers of the product. What evidence is there

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that the charges for fire indemnity are practically the same among the independent and competing companies? It may be stated at once that such uniformity exists to a very large degree. It may also be stated further that there are very good reasons for the existence of this uniformity, so far as it is determined by the burning rate and not by the expense of management and commissions. And further that a larger degree of uniformity would probably result in an improvement in the fire insurance business and ultimately in a lower cost of indemnity to property holders.

This calls for a brief explanation of how the rates are determined. This is an unexplainable mystery, it would seem, if the laws of several states and the complaints of some property holders are taken as criteria of the human understanding. Yet there is nothing mysterious about fire rates. While there is as much reason for difference in the premium for fire insurance policies among different companies, so far as the expense element of the charge is concerned, as there is among producers of other commodities, yet so far as the rate is determined by the actual loss or burning rate on different kinds of property, there should be no difference. No greater number of drug stores insured in one

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company will burn because they are insured in that company rather than in another company, provided the selection has been well made and the risks distributed. It is therefore not the expense rate, but the burning rate to which the explanation is directed. Why should cost be uniform in all companies for this element, and how is this cost determined?

Each industry, and therefore each class of property, should bear its costs of producing a commodity. Fire insurance is one of the elements in the cost of production. Therefore the burning rate in each industry should form the proper basis for the insurance charge. Under our system of state regulation of insurance and the insistence of some state legislatures that the burning rate in the particular state be taken as the basis, injustice may indeed result, because the number of plants or producing units may indeed be too few to form the basis for a fair average. Mutuality should be and must be the elementary principle in all insurance, but mutuality must have a sufficiently wide basis if it is to be just. But in fire insurance mutuality must also be restricted; that is to say, it should be limited to classes of property, but with a wide application within the

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class. It is advisable, then, to have a classification of property and a record of the losses on each class. Nor is the experience of one company sufficient to establish the rate, even if its experience extends for a long period and over the whole country. The combined experience of all companies on all classes of property can only afford a satisfactory basis for rate making.

The two systems generally used in this country for rating mercantile property are the Universal Mercantile Schedule and the Dean Schedule. These schedules apply to mercantile property which includes by far the most important risks, both as to value and number of risks. Other schedules are used, but in all of them there is the attempt to analyze the elements in a risk on the basis of its contribution to losses actual or potential. The rating of properties is usually not directly done by the insurance companies themselves, but by numerous rating bureaus found in all the important cities. These bureaus are independent of the companies and sell their service to the companies in the same manner that the makers of fire insurance maps do. It is the business of such bureaus to inspect properties which they rate and to make general surveys of cities for the purpose

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of establishing a rating for them, based upon such numerous elements as kinds of buildings, water systems, and the equipment of fire departments. Since their service is sold indiscriminately to all companies, there is no reason for them to overrate or underrate the risks. These facts, briefly stated, account for a large part of the uniformity in the rates of all companies so far as this is a uniformity determined by the burning rate. In other cases and on other classes of property the experience of companies forms the basis of the charge.

There have been many attempts to forbid the companies from exchanging their experiences. A number of states have passed Anti-Compact laws which seek to forbid companies from exchanging their experience and agreeing on rates. The intent of the framers of these laws has doubtless been good, and no doubt unlimited freedom in such matters should be restricted. Yet it is certainly desirable to have collected experience of such companies as a basis upon which to make fair rates. What is needed is not a law to prohibit such an exchange and such agreements, but to compel this exchange of experience and an agreement on rates under the supervision of the state.

The burning rate in fire insurance is a changing
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factor, due to the changing character of construction material, of building codes, and of improved protection. The public has witnessed the companies changing rates for one reason or another, now to a higher plane and now to a lower plane, and has immediately concluded that evil designs have been made by the companies against them. This may have been true in a number of cases, but in most cases it has been due only to the changing character of the risks.

The method of rating has been constantly improved, although no one claims for it perfection. Indeed there cannot be any perfect and closed rate established; for, as has been shown, the uncertain factors in the risk are continually changing. The most that can be expected or demanded is that rates be determined upon property in a scientific manner and that equity be secured between classes of property insured. In order to secure this end there must be available the experience of many companies on the different classes of risks, and an analysis of these losses made.

It would then appear that the chief element in the cost of fire indemnity, that is, the prime charge for property loss and not for expense, should be the same for all companies. There might be even

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then very good reasons for the enactment of anti-compact laws; but if such were the case, the purpose of enacting such laws should be somewhat different from that which the states that have such laws have had in mind.

There have been and now are agreements among companies as to the commission which a company should pay to an agent for securing the business, and it would seem that such agreements might be, under proper supervision, in the interests of the public rather than opposed to public policy as many suppose. A favorite device frequently employed by recently organized companies to secure business has been to offer high rates of commission. Rate wars have occurred among companies over a particular risk, the risks of a city or even a state, and as a result indemnity has sometimes been sold at far less than cost. After the contest was over rates have been advanced to a normal basis. It is not surprising that the public, which is not versed in the insurance business, has concluded that companies were conspiring against them when they have been told that a new policy on their property would cost more than the old one or when it was announced that rates for the city or district had been advanced without any

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apparent change in the character of the risks. The acts of the companies, quite as much as the ignorance of the public concerning insurance, have been responsible for the anti-compact laws of the various states. It may well be contended that the state would be justified in establishing a certain maximum of expense, especially in reference to the commission, which shall be permitted. If the state should establish, for example, 40 per cent as the maximum expense which would be permitted, this would undoubtedly make it difficult for some companies to continue in business and some would be forced to retire. But if other companies could meet this requirement and if sufficient indemnity would be offered for sale, there would seem to be no good reason why the public — the state — should be forced to subsidize inefficient insurance companies by permitting such a high rate of expense as would make it possible for any group of individuals to form an insurance company and continue to do business regardless of the rate of expense at which the business was transacted.

If commissions were also limited, this would, with the preceding general limitation on expense, make it more difficult for new companies to enter the field; but again if sufficient indemnity is

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offered for sale, and if competition is present and adequate regulation of rates has been secured, there is no reason why the public should be interested in having new companies formed.

The probable effect of such limitations would be to encourage the formation of a greater number of purely mutual fire insurance organizations and to secure the existence of a number of highly successful and efficient stock companies. Many would hold that such a situation would be preferable to the past condition with many new stock companies being formed, many of which have failed and entailed loss to the public both on the insurance purchased and the stock held.

Doubtless many officials of insurance companies would agree that commissions for writing the business have frequently been unnecessarily high. Agreements have been made and are now in force among some companies to regulate the commission paid, but it has always been difficult to secure coöperation on this subject and adherence to the agreement. Some of the older companies have refused to coöperate on this subject, and most of the new companies have refused to agree on commissions. The refusal is frequently made because offering the higher commission was the easiest

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method for the new company to secure the risks. It is an unfortunate kind of competition for which the public has been forced in the last analysis to pay. It is the same kind of "cut-throat" competition which prevailed in the railway business in the days when there were no state laws or state commissions to regulate rates.

It is believed that there are even better reasons for regulating commissions for selling fire insurance than for establishing railway rates. Certainly the difficulty in determining a fair and just price for the service rendered is not so great.

The companies themselves would still have ample opportunity to use their skill, foresight, and ability in reducing the other elements in the expense, securing better results from their investments, and in short so managing the company as to secure a profit for the stockholders and perhaps a lower charge to the public for the service. That is to state, the regulation of commissions, or even the total expense, would take away none of the important incentives which private business now has to secure profit for itself and to produce good service for the public.

To summarize, then, the evidence of monopoly as shown by agreements on rates. It is found that

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independent rating bureaus do most of the work in determining the rates on mercantile risks; that schedules for rating are used for certain classes of property in which an analysis of the elements in the risk is made, and finally that compulsory compact laws are needed to replace anti-compact laws. This would mean that the companies would be permitted to make their rates on the basis of the experience of losses of all companies on all classes of property under the supervision of the state.

There remains much to be done in securing scientific rates, and especially is greater equity in these rates to be desired; but the absence of these desirable ends does not prove the existence or danger of a monopoly in the fire insurance business. New companies are being formed. Foreign companies are admitted to the various states for the purpose of selling fire indemnity. Capital is flowing into and out of the business; for it does not take the form of such fixed capital as machinery, tools, or factories, which is the case in other industries. It retains its mobility. There would seem to be no necessity for the state to assume the business of fire insurance simply because the state is not now able to regulate it. The states have

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ample power in this respect, and whatever injustices and inequities there are in rates could no more easily be corrected by the state's assumption of the business than by exercising its wide power of regulating the business.

Indeed there would, under a state monopoly of the business, be a very strong inducement for the state to use its own experience as a basis for the determination of rates, and this geographical unit is much less satisfactory than a wider one. In fact the state would probably be forced to use such a unit, and such a unit is practically unworkable with justice to the insured. For example, the per capita fire loss in Ohio had fallen to \$1.20 in 1911, whereas in the United States it was almost \$3. Would not the people of Ohio insist that the state be taken as the unit of area for rate-making purposes under state insurance? Any satisfactory classification would scarcely be possible, owing to the limited number of representatives of an industry, unless a combination of risks should be made. One state might have but three flouring mills, and yet injustice might result if a large group of manufacturing plants should be used to form a class. Then, again, the loss owing to a conflagration in a city would entail a marked increase in rates

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for a single state. Consider but a moment the cost to the people of California if they were compelled to meet the losses due to the San Francisco earthquake and fire.

The truth of the matter regarding fire insurance rates is that they are very complex and present many more difficulties in arriving at and maintaining a fair charge than do many other services or commodities. Railway charges, for example, present no such difficulties as do fire insurance rates. The former have to do with more stationary elements.

Would the state be warranted in going into the fire insurance business for the purpose of more satisfactorily regulating it? It has been shown that the state has complete power of regulation. Supreme courts have time and again given expression to this fact. For example, the power of the legislature to delegate to a commissioner of insurance the right to deny admission to a foreign company or to withdraw the right to do business has been upheld. Some states have even gone to the extreme point of passing a law under which a foreign company forfeited its right to do business in the state in the event that it removed to the federal court a suit brought against it by a citizen

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of the state. Although this would seem to deny a right granted by the Constitution of the United States, yet such laws for all practical purposes are in operation.

It is not primarily a question of lack of power to regulate, but rather a question of how to regulate it. The rates may be too high in some cases and inequitable in other cases, but, judging by the character of legislation frequently enacted, there is little hope that the rates under a state monopoly would be absolutely just to all classes. As a matter of fact no means have been devised to secure absolutely scientific rates. If the state should discover such a means, it can force the companies to use it. There will doubtless be greater accuracy in determining rates as time goes on, but so long as the country is in process of rapidly changing its industrial life, so long will the numerous changing factors which go to make up fire insurance rate demand readjustments. That is to say, when our cities are built, when our industries become organized, and when our business experience is systemized, there will be that uniformity and standardization of processes and products which characterizes a stable industrial life. Industrially the country is yet in its infancy, and

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the growth to maturity must be accompanied by frequent changes and readjustments.

This is not to state that this coming stability will mean the absence of progress and therefore the disappearance of changes, but the changes will not be of a revolutionary, but of an evolutionary character. The readjustments will be more gradual and constructive in their character. A standard city, a standard building, and a standard fire department will then imply more definite things in fire insurance than they now do, and therefore standard rates will have a greater degree of accuracy in them.

There yet remains for investigation the third suggested reason for the state assuming the business of fire insurance, viz. the social interests which the state would be able to serve by assuming the business. This question must very largely be decided upon the possibility of reducing the fire loss or the fire waste under the state.

The following table shows the fire losses for the past 36 years:—

1912	. . .	\$225,320,900	1906	. . .	459,710,000
1911	. . .	234,337,250	1905	. . .	175,193,800
1910	. . .	234,470,650	1904	. . .	252,554,050
1909	. . .	203,649,200	1903	. . .	156,195,700
1908	. . .	238,562,250	1902	. . .	149,260,850
1907	. . .	215,671,250	1901	. . .	164,547,450

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1900	. . .	\$163,362,250	1888	. . .	110,885,000
1899	. . .	136,772,200	1887	. . .	120,283,000
1898	. . .	119,650,500	1886	. . .	104,924,000
1897	. . .	110,319,650	1885	. . .	102,818,700
1896	. . .	115,655,500	1884	. . .	110,008,600
1895	. . .	129,835,700	1883	. . .	110,149,000
1894	. . .	124,246,400	1882	. . .	84,515,000
1893	. . .	156,445,875	1881	. . .	81,280,000
1892	. . .	151,516,000	1880	. . .	74,643,400
1891	. . .	143,764,000	1879	. . .	77,703,700
1890	. . .	108,993,700	1878	. . .	64,315,900
1889	. . .	123,046,800	1877	. . .	68,265,800

This aggregates a total of \$5,406,666,325 for the thirty-six years, or an annual average loss of \$150,185,175.69. These statistics do not include the numerous losses which are never reported and upon which no insurance was carried. The statistics of the National Board of Fire Underwriters for 1911 show that the per capita loss for cities of 20,000 and over was \$2.62, an increase of twenty-three cents over 1910. A comparison for the United States as a whole shows that more than one third of the total loss is borne by one third of the population. The statistics also seem to show that as between urban and rural communities losses on property under the better class of protection have abnormally increased, while losses on property with poorer protection have grown less. This is a forceful commentary on the unpredictable character of the fire loss. Comparing the \$2.62 per capita

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loss in our cities with that in the cities of foreign countries the following results are shown. Eleven out of twelve of the largest cities in England had a per capita loss under one dollar. Belfast in Ireland had a loss of ninety-three cents per capita and Dublin thirteen cents; Aberdeen in Scotland had a loss of thirty-seven cents and Edinburgh a loss of sixty-six cents per capita; Marseilles in France had a loss of \$1.27 and Paris a loss of sixty cents; eight of the largest cities in Germany had a per capita loss that averaged twenty-three cents; six of the largest cities in Italy had an average per capita loss of thirty-one cents; Moscow in Russia, where wood is frequently used, had a per capita loss of \$1.46 and St. Petersburg ninety-three cents.

No country other than one of such enormous natural resources and vigorous population as the United States would be able to endure such losses by fire, and even in the United States the losses have become so great that serious attention must soon be given to their reduction. We have had such a large fund of natural wealth, and we have believed so thoroughly in individual liberty, that we have neither felt the need of economy in this particular, nor would we probably have been

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willing to circumscribe our personal liberties, even if we had recognized the uselessness of much of the loss. Timber has been abundant; the demand for new buildings has been pressing, and the increase in industrial development has been so great that any building erected would need soon to be replaced. We have preferred to permit construction and use under very few limitations. Our practice, if not supported by good theory, has been to build, to burn, and rebuild and burn, rather than to build a permanent building which would prove a loss either because it would soon be too small or because of the development of another section of the city or of another city.

This fire loss represents an enormous loss of social capital. It is a burden on present and future generations of which much is unnecessary. That there is insurance on the destroyed property reduces the burden only in part for the individual. The fact that other persons contribute to a fund from which the insured receives money to replace the destroyed property does not alter the essential fact that property has been forever destroyed. Yet the losses continue to increase until the problem has become one that should demand more attention. It is one of the really important

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aspects of the conservation problem of the country. It is sometimes offered as an indictment of private fire insurance, that this fire loss tends to increase. The following table shows the increase in losses by decades for the years 1880 to 1910, together with the increase in wealth.

YEARS	INCREASE IN WEALTH	PER CENT INCREASE	INCREASE IN INSURABLE PROPERTY	PER CENT INCREASE	INCREASE IN LOSS IN PROPERTY	PER CENT INCREASE
81-90	21,395,091,000	49	17,456,482,609	35.6		
91-00	23,480,215,775	36	33,412,378,537	50.4	294,674,675	28
01-10	18,586,905,142	20	91,600,352,352	90.7	898,246,125	66

A study of the table shows that the percentage of property insured has tended to increase very rapidly, so that an increasing proportion of the wealth is insured. Unfortunately the table shows that during the past decade the percentage of increase in the loss of property has been over three times the percentage increase in wealth. A desirable condition would be for the percentage increase of insured property to be greater than the percentage increase in wealth, and the percentage increase of loss in property to be less than the percentage increase in wealth.

The questions then arise, are these losses inevi-

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table and would they more probably be reduced under a system of state insurance than under private fire insurance? One of the determining factors in this unusually large fire loss is the fact that our buildings are so largely constructed of wood. Careless construction and occupancy, careless habits on the part of the public, as, for example, in their use of friction matches, ill-advised legislation, poor building codes, inadequate fire fighting equipment, each contributes to the loss, but each of these is more potent in causing the loss because our buildings are constructed of highly inflammable material. Over 60 per cent of our buildings are yet being constructed of wood, and so long as it is to the financial interest of an individual to build of wood, it will be only a question of how much the loss can be reduced. It is not necessary to make a harsh indictment of the American people for their materialism in this connection, for those of the human race who build of stone do so because this material is available, and therefore it is to their financial interests as individuals to do so. Analysis of the causes of fire made by a prominent insurance company and covering the losses for a period of the past nine years in 79,931 fires shows that lightning was

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responsible for 8.31 per cent of the losses, incendiary 4.90 per cent, carelessness 19.44 per cent, lighting 14.05 per cent, heating 21.06 per cent, vacancy .09 per cent, sparks 4.09 per cent, explosions, etc., 13.62 per cent, spontaneous combustion 2.77 per cent, rats and mice 1.30 per cent.

What do private insurance companies do to reduce this loss? Have they any interest in its reduction or is it their concern simply to assess the loss? Is it true, as is sometimes stated, that their interest stops with determining the premium, and that they would be interested in keeping the loss large, since this would mean more business to be transacted? Any one conversant with the practice of fire insurance companies knows that they do a vast amount of work which directly tends to reduce the fire loss. Not only are inspectors employed to investigate risks, but policyholders are advised as to methods of improving their risks in order to reduce the premium. Many companies have public service departments which give suggestions as to methods of construction which will secure a lower insurance rate on the property. Policies are canceled in risks when careless use of the property is discovered. It is true that much more inspection work might be done by the com-

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panies, but so long as all do not do it, competitive conditions prevent single companies from doing an unlimited amount of it, lest the cost be reflected in a higher rate than their competitors offer. Could not the state attack this problem of the fire loss with greater prospect of reducing it than is likely to occur under any plan of private insurance?

Would the justification be any greater for the state to do this in the event that it took over the business than that which now exists under a system of private insurance? To the extent that this work would be or is now undertaken, the interest and value to its citizens would form the basis for such activity. If the state took over the business, doubtless much of the work in reducing the unnecessary fire loss could be done in connection with the department of insurance. The concentration of the inspection work would probably be accompanied by economies over the present method; for there is now under competitive conditions some duplication, although the primary inspection and rating work, so far as it is done by Rating Bureaus, avoids much of the duplication. But the reduction of the unnecessary fire loss is not simply a question of better inspection work. It is a ques-

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tion partly of carelessness, partly of economic interest to the individual in building cheaper and more inflammable buildings, and partly of criminal acts. The causes therefore cannot be removed at once, for there is no mysterious power residing in the state by which the moral character and economic interests of man can be immediately changed. The state can probably do as much in reducing this under a system of private insurance as under state insurance. Whether the actual cost to the public would be less or greater, we have no means of deciding. In many states the people have already recognized the importance of the problem and are working on its solution. A number of states have established departments under the direction of a Fire Marshal. It is the duty of this official to inspect buildings and condemn them, and even destroy them if they are not safe to use. He may also order improvements to be made in buildings and order fire escapes placed on buildings. He investigates the causes of fires, collects and tabulates fire statistics, issues pamphlets on the subject of causes of fires, methods of preventing or controlling them, and in general conducts a campaign of public education in fire prevention. He also has, as an important duty,

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the discovery and prosecution of cases of willful destruction of property. This work is already showing its results in those states which have efficient departments of this character, but the work needs to be greatly developed, not only in each state now doing it, but each state should carry on work of this kind.

In Ohio the Fire Marshal's office was established in 1900, and a comparative statement of the fire losses by years for the decade is as follows:—

YEAR	NUMBER OF FIRES	LOSS
1901	7011	\$11,196,789
1902	5194	8,000,000
1903	6025	7,797,995
1904	5812	6,850,578
1905	4851	6,112,707
1906	4448	6,991,111
1907	4534	7,077,702
1908	5322	6,681,703
1909	4544	6,537,061
1910	4724	6,952,320

There can be no doubt of the social justification of the work, and its need would exist even under a system of state insurance. It is, however, necessary that the people who pay for the cost of such service, which reflects itself in a lower fire loss,

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should receive a return in lower premium charges on their insured property. This again suggests the necessity for a closer supervision of fire rates by the state if the system of private insurance is continued.

In connection with this subject of reducing the fire loss the valued-policy laws of a number of states arise. These laws provide in general that the sum named in the policy shall at the time of the fire be considered as conclusive evidence of the indemnity to be paid. These laws have probably raised very materially the cost of insurance, for they tempt the dishonest property owner to burn his property. Such laws are an incentive to dishonesty first, because they make it advantageous for the individual to misrepresent facts in order to secure insurance in excess of the actual value of the property, and second, in making it to his advantage to willfully burn his overvalued property.

Legislators have frequently made the mistake of placing the whole subject on a personal basis by arguing that it was of no one's concern if an individual wished to go into the insurance market and to purchase, for example, \$6000 worth of insurance. But insurance is not sold like potatoes. An insur-

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ance company sells indemnity. An individual might buy a bushel of potatoes when he needed only a peck without jeopardizing any public interest or doing an injury to another person, but an individual cannot purchase \$6000 worth of indemnity on \$4000 worth of property without doing all other honest buyers of insurance an injury. It means that the extra \$2000 must be donated by the other holders of insurance to the individual who suffered a \$4000 loss. Yet strange as it may seem, valued-policy laws and State Fire Marshals are found in the same state. Thus the state passes a law to make a thief and appoints by law an official to catch the thief.

The historical background which explains the valued-policy law is that in the early history of fire insurance the policy was limited in its terms to pay losses only to the amount of three fourths of the actual loss. But unscrupulous agents encouraged, especially in agricultural communities, an overinsurance which at the time of the loss could never be collected. The wrong needed to be righted, but the remedy was an absurd one. Something could be done to reduce the unnecessary fire loss by repealing these valued-policy laws and replacing them with laws requiring more careful

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inspection of property and more careful use of property.

Another law on the statute books of many states which also affects the fire loss is the anti-coinsurance law. Coinsurance is the plan by which the insured agrees to carry a part of the risk in case of a loss when the amount insured is not equal to a certain percentage of the property's value. It is just as important that property be not insured for too small a proportion of its value as not to be insured for more than its value. Rates cannot be scientifically and equitably fixed unless there is some uniformity in the basis of assessing the cost. The present method of determining rates is, as has been described, to make each individual risk contribute its equitable proportion of the total sum collected for loss payments. Each risk is credited with its good features and debited with its bad ones, thereby encouraging good building and occupancy. Suppose now that the rate thus determined is 1 per cent on a building worth \$50,000. This is done upon the assumption that the building will be insured for \$40,000, or 80 per cent of its value, and it will therefore contribute \$400 to the aggregate sum collected to pay losses. If the owner, however, purchases only \$20,000

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worth of indemnity, the contribution to the sum for losses will be only \$200 and the insurance company will be in error in its calculations 50 per cent. This 50 per cent error must be made up by other policyholders, and consequently the average rate which they pay must be increased. The point may be made clear by comparing the insurance rate with a tax rate. Suppose the value of the taxable property in a district is \$50,000,000 and the expenses to be met by taxation are \$1,000,000. If it levies a tax of 2 per cent, this sum will be raised. If, however, one fifth of the property holders who own \$10,000,000 worth of the property are permitted to enter their property for taxation at \$5,000,000 and the 2 per cent tax is collected, they will pay only \$100,000, whereas they should have paid \$200,000. The remaining property holders must pay the other \$100,000 if the total sum of \$1,000,000 for the community's expenses is to be raised. Just as in taxation, where it makes no great difference at what per cent of valuation the property is assessed, whether 100 per cent, 80 per cent, or 50 per cent, so it is uniform on all property, so in insurance rating it makes no great difference whether the property is valued at 100 per cent, 80 per cent, or 50 per cent, so long

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as it is uniform. Owing to the fact that the value of property frequently changes, it is the practice to base the rate on an 80 per cent valuation ; but any other rate would make possible scientific rating. For any value above the agreed, the owner is the insurer ; that is to state, he is a coinsurer with the company.

In Europe and in marine insurance, coinsurance is the rule, and there is scarcely any doubt that a system of state insurance would apply the principle of coinsurance. The coinsurance principle works no hardships on the owner in case either of a large or of a small loss if the amount of insurance which he carries is equal to or in excess of the percentage of the whole value of the property which the coinsurance clause demands. It only becomes a factor when there is a partial loss which destroys a smaller percentage of the value of the property than that agreed upon in the coinsurance clause. A repeal then by the states of the valued-policy and anti-coinsurance laws and greater supervision of rates would do something to bring about greater equity in rates and reduce the fire loss.

This suggests another reason assigned for a state monopoly of insurance, viz. to secure greater equity in rates. This means that if ideal equity is

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to be secured, there will be the complete absence of discrimination. Discrimination may occur between persons, between places, and between classes of property. So soon as one attempts to lay down an ideal system of making fire insurance rates which will be absolutely free from discrimination, it is very easy to criticize the plan both on the basis of theory and practice. It is easy to state that each class of property should bear its cost of fire indemnity, but there are endless problems in the matter of classification as well as in determining what the loss and the causes of the loss are. Absolute equity as between individuals does not exist in any business. The consumer is forced to purchase almost daily commodities at a price inequitable as compared with the price to some other purchases even in the same locality. He buys from his corner drug store an article which he could have purchased for much less than the cost of transportation to another place. His groceryman is continually raising and lowering his prices on a scale different from that of another groceryman in the same city.

In life insurance the individual pays a charge which has been determined previously by the mortality experience of those of similar physical

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conditions and the same age. But in fire insurance this charge is continually changing. Annual experience of losses on property must be supplemented with good underwriting judgment which should be the result of observing and studying past experience in order to secure fair fire insurance rates. Discriminations of every character cannot be removed, but some of them can be reduced. If careful analysis of losses on kinds of property is made, and if the experience extends over sufficient time, regions, and amounts of property, a basis for fair rates is supplied. Certainly little excuse could then be offered for discrimination between persons owning the same kind of property. Likewise discrimination among places on the same class of property could not be justified. Discriminations among classes of property are doubtless more difficult to avoid, but carefully tabulated experience of losses would hardly justify the difference on certain classes of property which now exists. It is in this connection that the state conduct of the business would make greatest change, but this result might as well be accomplished by the state under the present system of private insurance. It is probably because the public has but imperfectly recognized this defect and because

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of their general ignorance regarding insurance that these numerous examples of misdirected fire insurance legislation are found.

If the business of fire insurance is to continue under private ownership, it is necessary for those interested in it to cease uselessly complaining about the burden of insurance legislation and begin a campaign of educating the public. The companies must work out a system of closer coöperation and bring into the rates greater equity. The public is becoming more critical of all business, and its criticisms promise to be constructive rather than destructive. If competition and coöperation among companies cannot result in fair rates, there are but two choices. These are rates determined by the state for the companies or rates made by the state for its own monopoly of insurance. There is among insurance officials a disposition when the question of rate regulation by the state arises to dispose of the whole question by stating that it cannot be done. Yet in the case of railways it has been done and experiments are now being made in what practically amounts to making fire rates by the state. If these attempts should prove successful, and if private insurance does not make improvements both as to greater equity

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and in possible reductions in expense, state insurance may easily be the logical result.

The people are intrusting more and greater activities to the state, and the efficiency of government is increasing rapidly. In so far as this efficiency is shown by achieved results, in so far will the state commend itself to its citizens as worthy of being intrusted with new activities.

Some general considerations on the question of a state monopoly of fire insurance remain. If the insurance is made compulsory, the agency expense could doubtless be reduced. Viewed simply as an activity of the state for purely social benefit, there would seem to be no good reasons why fire insurance should not be made compulsory. Property exists and is subjected to the danger of a loss by fire, by means of which society is made to suffer. The value of the property is comparatively easy to determine. Insurance is the only method known by means of which the loss can be reduced. If a social risk exists and can thus be reduced by a well-known method, compulsion by the state for the social benefit has good grounds upon which to rest. Only the limited number of representatives of property in particular classes would be a bar

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for a determination of rates quite as accurate as and probably more so than those which now exist under private insurance. There would, however, be no reason why the state could not use the experiences of losses in other states to aid it in determining its rates unless practical politics or local sentiment and prejudice would insist upon a state experience of losses for rate making. A conflagration would probably present a difficult problem for a system of state insurance.

The state would accumulate a surplus, but such a surplus would not need to be as large as the aggregate surplus of the private companies. The concentration of the surplus would thus reduce its amount and leave in the possession of the public a part of the funds now collected. The sums not collected under state insurance would remain in private hands for productive purposes. It is true that the surplus now collected by private companies is loaned at interest and thus productively employed, but it is quite possible that something might be gained by permitting the excess to remain in the possession of the numerous contributors. The surplus collected by the state would also be productively employed if it were placed in financial institutions and loaned to the private investor.

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The particular disposition of this surplus and the form it would take would need to be carefully worked out. It would need to be in such a form as to realize quickly upon it. It might be placed in financial institutions which would pay to the state an interest upon it, from the interest which the financial institution received from loaning it. Just as in life insurance so in fire insurance the premium paid is spent for management, for commissions and other expenses, and for losses. If the first and second elements in the expense can be eliminated or reduced, the premium necessary to meet losses will be reduced. It is because the public is beginning to think that the possibility of such reductions exists, and because they think they have often not received fair treatment from private insurance, that they are agitating the subject of state insurance.

On this subject the words of Mr. Hotchkiss, late Superintendent of Insurance in New York, can be quoted with approval. "What is needed by our people is not submergence of this great institution in sovereignty, but the proper coördination of insurance and government. Each should do for the other only what each can do better than the other. In some things — underwriting and adjust-

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ment, for instance — insurance by private corporations has been eminently successful. These the state should, save for helpful supervision, let alone. But where corporate initiative has failed, the state should coördinate with its creatures. In some fields competitive practices prevent rate making that is level with economic cost. The temptation to withhold too much for salary or overhead charge, or to pay too much — often far too much — for business, is ever present. Hence home office disbursements, generally, and commission payments are, in some quarters, higher than can be justified by the service performed. As results, so-called gentlemen's agreements to maintain rates thus swollen are branded as trusts, and, despite their existence, rate wars are waged which profit the few, but postpone that adjustment of premium charge to economic cost which is essential to public satisfaction.

“ While leaving to its insurance corporations all technical and specialized functions and making no effort, save through proper watchfulness, to interfere with these factors in the rate charged, will not the state in the not distant future coördinate with corporate insurance and regulate or limit expenses of all kinds? If it does not, the present

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drift toward state insurance seems likely to continue. For, whatever be the field, the people will not long pay for the insurance of the future more than such service is rightly worth.”

III

SOCIAL INSURANCE

CHAPTER VI

THE NATURE OF SOCIAL INSURANCE

THE subject of Life and Fire Insurance has been considered with respect to the desirability of making of them a state monopoly, and there remains for discussion the subject of social insurance. In considering the several kinds of Social Insurance it will be necessary to base the discussion on the more general aspects and effects of such insurance rather than upon a detailed examination of its actual accomplishments. This is necessary because it is a newer application of the insurance principle, and no such scientific accuracy is to be found as in the longer established forms of life and fire insurance. Then, too, the various forms of social insurance are receiving great extensions from time to time, which causes readjustment of the basis upon which they are established. For example, a liability law may be replaced by a compensation law: an old age pension law may be changed to begin at age 55 in the place of age 65.

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The term "Social Insurance" in its widest sense includes all those applications of the insurance principle which protect the social organism against all the risks to which it is exposed. It is usually applied in a more restricted sense to include only those forms of insurance which protect the wage-earning class. In this discussion it will be understood to include Industrial Accident Insurance, Old Age and Invalidity Insurance, and Unemployment Insurance. The benefits resulting from an application of the insurance principle have been to a large extent limited to the property-owning class. This has been due chiefly to the fact that the applications of the insurance principle which in the past have been worked out have called, at least in the most scientific plans of its applications, for periodic payments of stated sums. The great masses of people, either because of lack of thrift or for reasons over which they have little or no control, have not had the sums to make the payments. They have, therefore, been forced either to depend upon such impracticable plans as assessments insurance, whose results have been disappointing, or to such expensive plans as private industrial insurance, whose cost has been so high that the insured received but a small part of the

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benefits which the total payments would have purchased if the expense of operating the business had not been so great. Assessment Insurance by its small collections did afford a relief to many, but history does not afford an example of any such society that has been able to continue as a successful organization. All have had to disappoint their members in the end. The numerous five and ten cent collections of industrial insurance have afforded a burial fund, but the expense of making these collections has been so great that the amounts left for policyholders made a pathetic commentary on the poverty of the poor.

The name, Social Insurance, is indicative of the purpose of such insurance and distinguishes it from other forms of insurance in which the private or personal interest predominates, in the thinking of the people, over the social interest. That such a term has come into general use implies that there has been a great development in the feeling of human solidarity. The community is beginning to realize that the burdens of a particular class should be borne by the collective strength of the community. The idea that the strong should assist in bearing the burdens of the weak is not only a result of the growth of humanitarian

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thinking, but it is also a result of more correct thinking upon the problem of what constitutes a strong nation and an efficient industrial community. It has come to be realized that in order to advance the prosperity of a nation, it is necessary to conserve its productive powers by some system of relieving the misfortunes of the deserving individual. What becomes to the individual a crushing burden is borne lightly by the whole community under a system of insurance. The underlying basis of social insurance is then neither charitable nor individualistic. The more fortunate economic classes, however philanthropically minded they may be, are not called upon, under a system of social insurance, to relieve an individual of his misfortune, but rather to pay the just share of what is rightly their costs, both as a consumer of goods and as members of the social group which must live with and among all other members. Therefore these more fortunate economic classes must be as social beings interested in whatever benefits other members of the group. Nor is the aid given to the individual as such. It is not granted on personal grounds. It is given because he is a member of the social community whose interests are to secure the efficiency in a

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social sense of every one of its members. Any element in the plan of social insurance which has a pauperizing effect upon the recipients is to be carefully avoided. Society has already paid too great a penalty for ill-devised plans of relief. The idea of social insurance is not to relieve individuals from the personal necessity of providing for the ordinary demands of life. His food, his clothing, his home, and his family must have his individual care, and there remains this adequate stimulus for thrift in providing for his ordinary wants. It is only for exceptional demands, as in case of accident, sickness, old age, and unemployment, that society is to be called upon to assist in a collective manner the individual to provide for his needs. Security from these exceptional risks will enable better provisions to be made for the ordinary demands upon the individual, and the stimulus of saving for these purposes will be preserved.

If such is the general character of Social Insurance, then the relation of the state to it will be somewhat different than to the other forms of insurance which have been discussed. That is to say, if the term "social" is applicable, it cannot be considered a business from which profit should

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be derived to the same degree as is true in the case of a purely private business. What is a social concern, a social duty, should not be used as a source of private revenue. It is proposed, then, to examine the particular character of the various forms of social insurance with the view of determining the relation of the state to such forms of insurance. The best known form of insurance of this character is Industrial Insurance, but this term for our purpose does not refer to the industrial insurance sold by private companies, which was chiefly used to supply a burial fund, but to industrial accident insurance or liability insurance. The theory underlying liability for payment to employees by employers is of very ancient origin, but industrial conditions have changed so rapidly and so completely that circumstances warranted a much more rapid change in the theory than has actually occurred.

Before discussing each of these methods, it is important to understand how the evolution of industrial society has caused the need of, and the demand for, insurance for the wage earners to arise. In ancient and medieval times the social and industrial organizations precluded the existence of insurance for the wage earner. Indeed,

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there was no such class of wage earners as we now know them. During the existence of slavery a large part of the work was done by this class, and as the slave was considered a species of property, nothing was owed to him by his employer or owner. He cared for him, not so much as a duty, but because it was to his economic interest to do so. The comparatively simple industrial life of the early times gave little value to the life of an individual as such. During medieval times the feudal system prevailed, and the masses of people, although having in many cases comparatively few rights, enjoyed protection from their lords. The hierachal form of social organization gave a definite status to each member of the social group. Later, when the trade and labor classes had freed themselves from their dependence, guilds and fraternities arose. One of the most important purposes of these organizations was to care for their members in times of sickness and for the deceased member's family in case of death. The first classes to secure independence were the commercial and trade classes of the free cities, and as capital developed they assumed gradually a position of greater independence and importance.

Capital was being accumulated from the ac-

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tivities of the trading and commercial classes. The discovery of gold and silver in the new world supplied a stock of metals upon which a money economy could be established. The age of discovery opened up new lands for exploitation and brought into existence new commodities and new markets. The whole industrial world was on the eve of a revolution as a result of the accumulated capital, the stock of metals, and the new markets. This so-called industrial revolution is usually said to date from 1785 to 1825, but this period marks only the dates between which the transfer to a new industrial system was most rapid in England. The changes were so very marked that the word "revolution" may be applied to this period in England, but in other European countries and in the United States no such rapid changes occurred. It will be more accurate to call the change an evolution rather than a revolution and fix the dates to include the seventeenth, eighteenth, and the first half of the nineteenth centuries, because during this period the capitalistic system was fully established in the European and American countries. The feudal system had disappeared, the household or domestic system arose which the previous accumulation of capital made possible

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and the new markets made desirable. But the most important for our purpose, the status of the laborer was radically changed.

The laborer lost his tool and gained the machine, which, on account of its high cost, was beyond the powers of his private possession. He lost his personal master, and gained the impersonal corporation. The conditions of labor were now to be determined, not by two persons, the laborer and his master, but by one person and a thing. The laborer gave up the workshop of the home and went into the factory. He worked for a money wage under a wage contract. He was no longer a capitalist and a laborer, but simply a laborer selling his only possession — time. In the unprecedented demand for goods it is not surprising that the capitalistic class were often unmindful of the duties which they owed to the laborer as a man.

We need not rehearse how the humanitarian ideas slowly developed and how they gradually became expressed in various measures designed to protect the wage-earning class; nor what efforts were made by the wage earners themselves, through the formation of friendly societies and trade-unions, to protect themselves; nor how there came to be a labor question and why the neglect

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of the labor class during this period of the industrial evolution has caused the problem to become so acute in the present; nor how England, because she was the farthest developed industrially, began to enact laws for the protection of the labor class early in the nineteenth century and how other nations have followed her example. For our purpose it is sufficient to understand that the character of the industrial organization of the present demands institutions designed particularly for the industrial classes.

The relation of laborers to the employers in ancient and medieval times was quite different from what it has come to be in modern industrial times. The factory system was not in existence, and the bond of relation between the laborer and the employer was closer. The personal relation was more definite. In most cases the number of employees of one person was limited. The laborers worked for a person, not for a corporation. Out of this relationship of early times there grew up a common-law principle of liability of the employer to his employees, which, although it did not secure full protection to the laborers, yet was thought sufficient until late in the nineteenth century, when the common-law principle became ex-

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pressed in statute law. No greater proof of the helplessness or disadvantage at which the laborer bargains with the capitalist for his wage is to be found than in the fact that it was over a century after the establishment of the factory system before an employer's liability law was enacted. Dependence was placed in the operation of the common-law principle which had grown up from very early times.

We naturally look for the most definite expression of this principle in Roman law. We find that the master under this law was not only responsible to the servant for any injury suffered by the latter when not due to the employee's carelessness, but the master was also subject to liability for an injury suffered by a third party as a result of the actions of the servant when in the employment of the master. It is important to understand, however, that as the principle of liability developed under Roman and later under English law the liability did not rest upon the master in the following cases: first, if the person injured was a fellow-servant. This is known as the fellow-servant doctrine. Second, if the employee knew or had means of knowing the dangers incident to the employment and voluntarily

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accepted the employment. This is known as the assumed risk doctrine. Third, if the injury resulted from the combined negligence of employer and employee, that is, the latter contributed to the negligence which resulted in his injury. This is known as the contributory negligence doctrine.

It is important to understand these limitations or exceptions, because practically all the legislation and all the court decisions since this far-distant date, so far as they have given greater protection to the employees, have done so by modifying or doing away with these limitations. This is the goal from which we have started, and the goal to which we go is to assess upon society in some manner the total costs of production; to secure for the laborer, not only an adequate daily wage, but also protection against accident, however caused, against sickness, unemployment, invalidity, and old age. Not until then will many agree that an equitable system of distribution has been devised, for the burden now resting upon the shoulders of the laborer is not all his own.

Without tracing the changes in the conditions of work and the changes which occurred in the industrial organization after the establishment of the factory system, it may at once be stated that

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as a result of these changes England passed an employer's liability law in 1880. England was the most advanced industrial nation, and this fact, together with the character of its people and government, accounts for this law. The most surprising fact about the law is that its enactment was so long delayed both in Europe and in America.

In the United States the development of the idea of the obligation on society to bear the cost of industrial accidents has been slow in gaining acceptance. This has been due in part to the character of the industrial life and in part to the prevailing individualistic philosophy, which has very naturally received expression in our constitutions and laws. Industrially the country has been very largely agricultural, and the opportunity for free enterprise has been very great. There was a large amount of free land, and the worker had a choice of occupations. But as cities began to grow into great industrial centers, with all the concomitant problems of the factory system, a relationship of employer and employee arose, for which the old individualistic philosophy did not provide. Industrial accidents became numerous, and yet the right of free contract, the rights of

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private property, and other guarantees of the individualistic philosophy embodied in constitutions and laws, prevented a just assumption of what was a social burden. To state that wage earners are receiving a higher wage than formerly is not pertinent to the question, any more than to state that they are thriftless. Even if these statements are true, the question is, have wage earners shared equitably in the increased progress of the century, and are sufficient opportunities and inducements present to make them provident? The heavy burdens which they have borne as a result of accidents in their employment have resulted not simply because they were working for a wage for themselves, but also because they were producing commodities for society. In the second place the opportunity to own land or homes or the tools of production is very largely absent, and a powerful incentive to save is therefore absent. Whenever the result of saving can express itself in a tangible form, the inducement to save, especially to the less well educated, is very strong. The indefinite need for an old age which many may never experience, and which is far distant for all, the opportunity for an advanced education whose benefits are generally unknown because experi-

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enced by but few, the opportunity for leisure, which they do not know how to use because of the necessity of daily and continuous labor, these, and many other causes, have all been responsible for the absence of thrift among the laboring class, and have prevented them from adequately sharing in the wonderful progress of the past century.

There is, however, evidence of a great awakening among the people of the United States in regard to their duties to the wage-earning population. This is due in part to the great development of humanitarian thinking, and in part due to the gradual growth of class consciousness among wage earners, which has expressed itself in unified demands upon the public to be relieved of some of the burdens of society which the laborers have been carrying. For our purpose this demand has taken the form of an insistence that the old theory of employer's liability should be changed to meet the changed industrial conditions. There is but little justification under our present industrial organization for an insistence upon the old doctrines of assumed risk, fellow-servant, or contributory negligence, however deeply imbedded they are in laws and court decisions. In some states these doctrines have practically been abol-

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ished, and hence arises the need of distinguishing between the Employer's Liability principle and the Compensation principle.

The first principle has to do with the circumstances under which an employee could receive damages from his employer because the employer was made by law responsible for injuries received. This was, as has been shown, based upon the individualistic philosophy of the rights of property, of free competition, and contract. The second principle has to do with the compensation given either directly by the state or enforced by a law upon the employer to grant compensation for all injuries received while engaged in the services of an employer. It is true that the second principle may exclude certain industries, as, for example, agriculture or employers of a limited number of workmen, but the idea underlying the principle is to recognize that the large per cent of injuries received in industrial employment are not primarily due to the fault of the worker; that they are a just part of the costs of production, and society which uses the product should pay all its costs of production. If a workman in walking across a perfectly smooth factory floor should stumble and fall into a machine and as a result

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be under the necessity of having an arm amputated, he might not under a liability principle receive any damages from his employer, but under the compensation principle he would be indemnified on the ground that such accidents are possible to a workman, and that the loss should fall neither upon the employee nor the employer, but upon society for whom the product was being produced. The compensation principle is thus more inclusive than the liability principle, and its general adoption is probably only a question of a few years in those civilized countries where it is now partly in force.

CHAPTER VII

SHOULD THE STATE MONOPOLIZE SOCIAL INSURANCE ?

THE chief subject of the investigation is thus reached in the question, what instrumentality should be used to apply this principle? Should it be the state or private companies under the supervision of the state? It is well, in attempting an answer to this question, to investigate briefly the means which have been used to secure protection to the working classes from industrial accidents and sickness. One of the earliest methods of securing this protection, and one that has continued to the present time, is that whereby the employees formed among themselves purely mutual associations. When an accident or any other misfortune occurred, payments were made or aid rendered to the suffering worker by his associates. These mutual associations have been formed for various purposes and on various bases. Sometimes a stated sum without reference to the

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wage received was paid by each. Out of this, certain sums were paid during sickness or upon death. In other cases the collections and payments were adjusted to the wage received. Whatever the basis, the characteristic of all these associations was their mutuality. It was a voluntary association of workers usually employed in the same industry. They were not formed in response to any liability law of the state, but were simple expressions of the recognition on the part of the wage earners of their class interests. As a class they suffered certain misfortunes as a result of their employment, and they took this means of aiding each other. These societies exist in large numbers at present, and any plan of social insurance which does not take their existence into consideration and offer encouragement to their continuance and their improvement to a more scientific basis is likely to do a great social injury. These voluntary organizations would form, because they are voluntary and not compulsory, a means by which great social and industrial efficiency can be secured for this class of the population. They exist as a nucleus around which may gather many forces for growth. The state is a mysterious force for good only in so far as it works

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through the people who compose it, and social improvement cannot result from merely passing compulsory laws and attaching penalties for their disobedience, but rather by offering stimulus to desirable voluntary forces and organizations which spring out of the life and the experience of its citizens.

As the principle of liability of the employer to the worker became extended and better expressed in laws, private insurance organizations were formed which sold to the employer protection against claims made by the worker under the liability laws. This may be called public voluntary liability insurance. That is to state, the law established the liability, and the employer voluntarily purchased the protection of a private company which was formed to protect him against any suits which were entered by the workman for damages as a result of an industrial accident. These private companies established their charge or premium on the basis of the risks of the industry and the accidents in the particular plant. That is to state, the number of accidents in the industry and in the particular plant of the employer were the fundamental factors which determined the cost of the insurance or protection from damage

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suits for the particular employer. When a suit was entered by the workman, it was a matter of concern for the insurance company and not for the employer. The latter simply reported the facts to the insurance company, which either effected a settlement with the injured workman before a suit for damages was instituted and tried, or defended the case before the court and paid whatever damages were granted. This method of assuming liability under the law has come into very general use during the past thirty years. It has adaptability from the viewpoint of both employers and the insurance companies to any type of a liability or even a compensation law. The extent to which it has been satisfactory to the workingmen will be discussed later.

In addition to the above methods of securing protection to the working class another method has been developed of late years. This is the Relief Association, as exemplified in the associations of a number of important railway companies and large industrial organizations, such as the United States Steel Company and the International Harvester Company. These Relief Associations differ somewhat in the particulars of their organization and operation, but the purpose

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is largely the same. Not only is the worker granted aid in time of sickness and accident, but usually a pension is paid after a certain age, or in case of total disability, or to his family in case of death. The employee usually shares with the employer the cost of the service, although the latter may pay a large part or all of it in a few cases. Membership in the association is voluntary for the employee. The relief is adjusted to the wage received, and the systems in practically all cases have been carefully devised and operated.

Before passing to a consideration of the compensation principle it is well to note that the voluntary principle has been very largely the rule until the past several years. That is to state, the employer and the employee were permitted to take whatever means they chose to protect themselves against industrial sickness and accidents. The employees might ally themselves in mutual organizations; the employers could buy their liability protection from a private company selling such protection. Even when it was found that a considerable number of accidents was due to the nature of the industry itself and the demand arose that the industry, that is, the employer, be made liable for them, there was no attempt to

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dictate the manner in which this liability should be met. In other words the employer's liability principle as a legal principle had reached its limit. It was soon found, however, from practical results, that the condition of the employee had been but little improved. Liability in law had been established. The legal problem had been solved, but the social problem remained. The workman, it was found, could receive damages at law only after long delays and heavy expenses, which often absorbed a great part of the damages which were awarded. Suits were contested, and too often the success in resisting claims measured the excellence of the insurance company from the standpoint of the employer. At the close of 1911 the statistics of the Liability Companies reporting to the Massachusetts Department of Insurance showed that these companies had outstanding 14,227 suits.

For each of the preceding five years the suits unsettled for the year were as follows: 3394 suits unsettled for the year 1911; 5559 suits for 1910 unsettled; 2684 suits for 1909 unsettled; 1206 suits from 1908 unsettled; and 618 suits from 1907 unsettled. It is true that neither the total number of suits unsettled nor the suits of any one

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year are a large percentage of the total claims paid or the total claims in force for the year. But it is not in this fact that the chief significance lies. The real importance consists in this fact: that many workmen were injured and the indemnity belonging to them from some one was being withheld. They and their families needed to be supported in some manner from some source. Not the number of workmen injured in an industry has been the real measure of charges to the employer by the insurance company, but the amount of the claims which they were forced to pay constituted essentially the determinant of the premium. In a system, then, under which both the company and the employer had an advantage to gain from preventing the employee from securing indemnity, the results secured for the working-man were not large. Investigations made with some considerable care seem to warrant the statement that the workman has secured actually less than one third of the indemnity granted by the courts. What per cent he has secured of what he really should have secured as the result of an injury suffered through no fault of his own is certainly much less. Even under the best liability laws many injured workmen have either

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received nothing or have been persuaded to accept pathetically small amounts, or if the court has awarded damages, a large part of it has been taken to pay the costs of prosecuting the claim.

It is not then surprising that a demand arose to replace the indefinite liability laws under which the intended beneficiary — the workman — received so little, with a definite compensation law under which specific sums were to be paid upon the happening of certain industrial accidents. Such laws, by specifying the indemnity to be paid, avoid the necessity of numerous trials at law to fix either the responsibility for the injury or the amount to be paid. This introduces necessarily the system of compulsory insurance, but it does not follow that there need be compulsory organization. That is to state, the compensation may be established by law in great detail, and yet the employer might be left to make whatever arrangement he chose to meet the costs of paying the compensation.

That the insurance should be compulsory, however provided for, rests chiefly upon two points. First, the experience of the past seems to show that the workingman has not been able to secure protection against risks which were under-

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taken in the production of goods for society. Second, for whatever reasons, the facts show that he has not provided a fund from his earnings to care for himself and his family during the time that he has suffered from these accidents. Society therefore finds a large number of its members dependant upon it for certain periods, during which times they are either insufficiently cared for or are the subjects of forms of relief which in neither case tend to increase their social and industrial efficiency. Wage earners have neither the prudence nor the income to provide such insurance, nor have they the power to enforce employers to pay for it in the form of a higher wage. The insurance provided in compensation laws is therefore so thoroughly social and the practical results under a voluntary system of liability insurance have been so disappointing, that both on grounds of theory and practice it should be compulsory. The movement for compulsory insurance of this character has been realized in many European countries and is being adopted in the states of this country. The important questions thus are, should this form of insurance be made not only compulsory, but should it also be made the subject of a state monopoly?

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Most of the important European countries have made this form of insurance compulsory, and it would seem that the character of the insurance and the class to which it refers make compulsion the only possible working basis. The object of such insurance is to bring its benefits to those who need it most, but so long as it is voluntary the class which needs it most is not likely to secure it. It is true that certain classes, such as the paupers, the physically and mentally deficient, cannot be reached by such insurance, but the problem arising in connection with them is for philanthropy, for industrial education, and eugenics. The compulsion in the case of social insurance of this kind is merely to secure a form of social coöperation and cannot be considered an odious exercise of sovereignty. The wage earners have not protected themselves against the industrial risks. This may have been due to lack of means, ability to save, foresight, or a number of other causes, and only a plan of compulsion seems adequate for the work to be done.

If the state establishes a monopoly, it must be either to secure adequate regulation or for social-developmental purposes, and not with the hope of securing from such a monopoly any financial

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return. Little justification could be found in the principles of state financing for using this insurance as a source of revenue for the state. The wage earners as a class have little property to bear a tax, and their wages are far removed from that point which is supposed to justify a tax. The employer who directly pays the premium necessary to purchase this industrial insurance should not be required to pay more than the cost of the service, since a good system of taxation will levy a tax upon all his property. The accidents which occur in his plant are incurred in producing goods for social consumption, and his outlay should be limited to the costs of the materials and labor. Society could have nothing to gain by charging itself more than the full cost of making the industrial goods and thus use this insurance as a source of profit. Therefore no one of the three possible sources of a revenue can be used to make a profit for the state under a monopoly of this insurance. The wage earner whom the insurance is primarily intended to benefit cannot be used as a source of profit if a system should be desired of making him pay its costs; for a profit of this character would tend to defeat the very purpose of the insurance. The employer should not be used as a

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source of profit for the state since he is under a just system of taxation already contributing his share to the state's revenue. Lastly, society or the consumers of the product should not be used as a means of securing a profit, for this would be but taking money out of one pocket and placing it in another. Consumers should pay the full costs of producing the product, but not more than this. Other more direct and equitable methods of securing revenue to the state are available.

It may be urged, however, that it is for purposes of satisfactorily regulating the business that a state monopoly is desirable. This assumes that the results desired under a compensation law are difficult to secure under a system of state regulation of private insurance. That is to state, that even when the particular compensation is fixed by law, the results to the wage earner are not so good as when the law is administered and operated by the state. There is, in fact, no lack of statute power to regulate the private companies which would sell insurance under a compensation law. A state is supreme in the matter of regulating insurance transactions within the state. The particular regulations may not accomplish their purpose, but this is not due to a lack of power to

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regulate, but either to a lack of knowledge of how to regulate or to the peculiar character of the subject regulated. Complaint has been made in some states where compensation laws are in force that the private companies which sold the insurance protection increased the rates as compared with those in other states. But the state can regulate the rates or enforce rates of its own making. It is not because of any lack of constitutional power to regulate the private companies that a state monopoly should be urged, but rather for a number of other reasons which now demand consideration.

It is argued that private companies have, on the basis of their conduct of liability insurance, forfeited any right to claim that they can furnish the insurance under a compensation law either economically or equitably. The expenses of operating such companies in the United States have been shown to be about fifty per cent of the receipts, excluding profits to stockholders, while in Germany, where the state largely administers the law, such expenses are as low as 14.1 per cent of the receipts. The enormous expenses now paid for commission, salaries, and advertising would, it is claimed, be saved under a state monopoly.

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It is again pointed out that competition often results in discrimination in rates. The large employer, it is claimed, has always been able to secure more favorable rates than the small one after all fair allowance for the difference in writing and operating the business has been made. It is said that discrimination often occurs between the producers in different states. Rates are juggled to meet competition at one place or another. It is said dishonesty is prevalent among agents in rating risks, and that this is countenanced by the officials of the company as a necessary means of getting business under the conditions of competition.

Again it is pointed out that the private companies have never succeeded in forming associations to exchange experience from which really scientific rates could be made. Readjustments of rates to get the business have been more often the rule rather than rates based upon actual experience of losses.

It is also argued that under the private system there has not been the proper inducement given to improve the working condition of the plant; that is to say, the employer has had little inducement to install protective devices for his workmen

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because he knew that if the liability company attempted to raise his rates, another company would write his business either at the old rate or at a lower one. It is also urged that under a private system the compensation principle is likely not to be as satisfactory, owing to the fact that the worker will be forced to deal with his employer and a stranger whom his past experience has taught him to believe are not interested in securing justice for him, whereas he would feel that the state had no interests other than justice to serve. The private companies under the liability principle certainly have not earned great credit to themselves either for the economical use of the funds which they received or for their zeal in endeavoring to see that the injured worker secured the indemnity. Indeed it was not to be expected under the old system of liability that the insurance company should serve the workingmen. The company was paid a price to relieve the employer of the liability, and the company was the servant of the employer to protect him from the workman. The company could not at the same time be a protector to the employer against his workmen and a preserver of the interests of the workmen. Whatever the theory of liability in-

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surance has been, in its actual working, the private company has resisted the claims of the wage earner against the employer. It is therefore claimed that the interest of society in the workmen can be best served under such a state monopoly of the business.

It is true that the theory of compensation laws is that the costs of the insurance will be ultimately borne by the consumers of the product, and hence the important social interest of having a minimum cost in transacting the insurance. There are, however, some difficulties in a complete acceptance of the theory that the consumer will in every case bear all the costs of compensations for the injured workman. It is assumed that it is immaterial to the employer, or even to the private insurance company, what compensation is established, since each will but add it to the cost of producing the commodity, or the cost of the insurance and then collect it from the consumer. But is it always possible to shift completely this added cost? If a uniform compensation law for the whole country was adopted, such a shifting would undoubtedly be more possible. It may, however, happen that this increased cost of production may be the deciding factor in the competition between

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two producers in different states, having either different compensation laws, or where one has a compensation law and the other a liability law.

The cost of this insurance, which may be considered as a tax in discussing its incidence, is assumed to be a tax on consumption, and like all such taxes of this character its final incidence is difficult to determine. It has been pointed out that while a tax or charge of this character can be added to the price of one or more articles, yet such a tax on all commodities cannot raise the price of all articles. If this added charge in cost of the insurance be applied indiscriminately under competitive conditions to producers in the United States, the possibility of its shifting to consumers would be much greater than by a system under which only a part of the competitive producers would be assessed the cost of such insurance. The enacted and proposed compensation laws apply only to certain states, and even in the states which have such laws there are certain differences in the law. Many other states have no such laws, and judging from the general absence of uniformity in the legislation of the various states, and especially in the social legislation, this difference is likely to continue in the legislation for

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the protection of the wage earner. It is therefore not at all certain that the producer who immediately pays the cost of the insurance will be able, as the theory of such insurance assumes, to shift the tax or the cost of the insurance to the consumer in the form of a higher price for the commodity. The consumer is frequently, in these days of developed transportation facilities, interstate markets, and interstate business organizations, under no necessity to purchase the product from a producer within his state. Indeed it is the exception for a producer to derive his articles of consumption from the state of his residence. The day of local markets has passed. When green vegetables and perishable goods of all descriptions are transported hundreds of miles to markets, the local producer finds his only important control of the local market in his control over price.

There are but three sources from which the cost of the insurance can be paid, viz. from the profits of the producer, from the wages of the employee, and from the consumer in the form of a higher price. If the cost is taken from wages, the very purpose of the insurance will be counteracted, since the purpose of such insurance is to bring

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about an improvement in the condition of the wage earner.

It remains then to discuss the conditions under which the cost might be taken from the profits or from the price to the consumer. This calls for an examination of the conditions of production both as to the prevalence of competition or monopoly and also as to conditions of production; that is, whether it is subject to the laws of constant, decreasing, or increasing cost as well as to the nature of the demand, whether elastic or inelastic. The possibility and desirability of shifting the tax will be determined both by the conditions of cost under which it is produced and the character of the demand. That is to state, it may be produced under conditions of constant, decreasing, or increasing cost, and the demand for it may be elastic or inelastic. The simplest case is that where each unit is produced at a uniform cost; that is, the expenses of production neither increase nor decrease greatly as the number of units produced is increased or decreased. Producer A in state X, where there is a compensation law, would normally seek to shift the cost of the insurance to the consumer, but his competitor B in state Y, which either has no compensation law

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or one levying a lower charge, might be able to supply the consumers of A with the commodity at A's old price. A would then be forced to pay the cost of the insurance from profits or attempt to take it from wages. If A has been enjoying large profits, which means that competition has not been freely working, he may pay the cost and yet continue to do a profitable business. The second case is when the commodity is produced under conditions of increasing cost. Normally a tax on consumption under this condition does not, in strict theory, raise the price by the full amount of the tax, since a rise in price can only come with a decline in quantity produced, because a lowering in quantity produced means a lowering of the margin of cultivation or a lowering of the marginal cost. If, then, the cost is added to the former price, and the demand is so elastic that a smaller number of units are produced, the tax or cost added is counteracted in part by the decreased pressure on the source of supply. If producer A in state X then attempts to add the cost of the insurance to his former price, his competitor B in state Y may secure a part of his market, since A can only afford to add the cost to the normal price of the article by reducing the

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units he produces and thus securing the economies which come by lowering the marginal cost. Under these circumstances an incentive would be given to small-scale production.

In the case where cost is subject to conditions of increasing returns, a tax on consumption may in strict theory raise the price by the amount of the tax or even more. This is primarily due to the fact that the rise in price checks consumption under a condition of little elasticity of the demand; the supply is reduced and the cost per unit is increased, since under the hypothesis an increase in the units produced was accompanied by a decreased cost of production per unit. If, however, the demand is very inelastic, a condition not usually found in the case of articles produced under conditions of increasing returns, the tax or the cost of the insurance might be added to the price of the product. However, it is necessary to consider the competitor B in state Y, who is not compelled to increase his price. If A attempts to add the cost to the price of the article, B has very great inducements to offer A's patrons the article at the old price, since an increase in the units he produces, under the hypothesis, brings a decrease in the cost per unit. This would be

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true if the demand for the article was elastic, and B might stimulate its increased consumption by offering it at a lower price than A's old price, since he has already secured economies through the greater number of units produced by selling to A's old customers. Under such circumstances a powerful stimulus would be given to develop large-scale production in state Y by the laws of state X.

There remains the condition of monopoly in production to investigate. If the producer A in X is not subject to competition, but enjoys a monopoly or semi-monopoly, he is in greater control of price. As a monopolist he is presumed to have so adjusted his price as to yield him the maximum profit. A tax on monopoly profits cannot be shifted, but the cost of the insurance cannot be viewed as a tax on monopoly profits. It is assumed that it will be added to the price and borne by the consumer. Will it be to the interest of the monopolist to do this? If the demand is elastic and a rise in price from the addition of the cost of the insurance causes a decline in the units consumed, the monopolist may be quite willing to bear a part or all of the tax. This would especially be true if the monopolist was producing the article under

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conditions of increasing returns. If the demand is inelastic and the addition of the cost of the insurance to the price does not result in a decreased demand, the monopolist is likely to shift the cost to the producer. If he is producing under conditions of decreasing returns, he may be quite willing to add the price and accept a reduction in demand, since this may lessen costs for him. If the monopoly is of a public character, the force of a customary price and the power of the state over the rates or prices of the service may prevent the monopolist from increasing his price in order to shift the cost of the insurance, as the theory assumes all producers will do. However, too great refinement in analysis should be avoided in attempting to determine the bearer of the cost of this insurance. In this discussion the existence of the competitive producer B in Y state is the significant factor. It is assumed that he is free from this insurance charge, and this difference in his favor always exists as an immediate advantage, whatever the conditions of production and whatever the character of the demand.

The possibility of securing increased efficiency of the laborer, and therefore lowering the ultimate costs, must be considered in connection with this

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increased cost of production and the cost of living for the laborer. Yet the workman is not a consumer to the same extent as he is a producer in this particular. However, the increased efficiency would show itself only after a time and could hardly be expected to apply only to a state which had the particular compensation law. If the laws were uniform for the whole country, the argument of increased efficiency would more forcefully apply, but so long as there would be difference in such laws, it is difficult to understand how chaos and confusion in costs of production can be avoided. It may be argued that the existence of a good compensation law would attract a high grade of laborers to that state, and hence greater efficiency would be secured, because the employer could select his laborers. But labor is scarcely so mobile as to secure that result, and even if it was, the state would have the problem of dealing with the large number of inefficient who were left over after the assumed selective process had been completed. A state would have no power to apply a protective tariff labor policy by which to protect its producers. The United States might wisely use the protection principle in this connection if a uniform compensation law was enacted. The

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argument that the costs of compensation can be immediately shifted is somewhat superficial and fallacious when a careful analysis of the organization of production and distribution of goods is made. Goods are cheaply and quickly shipped long distance under our efficient system of interstate transportation.

It may be replied that the state can save enough by making a monopoly of the business to meet the difference in costs of production between a producer in that state and one in a state which does not have a compensation law. If the state makes the law not only compulsory, but also makes insurance in the state department compulsory, doubtless a considerable saving can be effected in agency and operating expense. It is also true that under a good compensation law employers would be relieved from paying out large sums for special funds, hospitals, gifts to people in distress, and charitable institutions. This might well happen to a certain extent, but it is questionable whether it is desirable for the state to discount the philanthropic motives of its citizens, if it establishes such a monopoly for purely social purposes. It is also argued that the enactment of such a law, particularly if the state operates the law under a

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department of state, will bring great improvements in the relation of employer and employee; that labor trouble will be decreased and the interest of the employee in his work will be stimulated. In short that efficiency will be greatly increased. Undoubtedly the old system of liability insurance in its practical working has done much to embitter the wage earner against his employer and society, but the real labor problem is too fundamental to be solved by any such temporary and trivial remedy.

It is proposed under a state monopoly to furnish the protection to the employer at cost, but however great the difference between that cost and the cost under a system of compulsory state compensation under private companies, the essential difficulty arises between the production cost to an employer in one state as compared to the production cost of a competing employer in another state. If one is to judge from the experience of the states which have enacted social legislation in the past, it would be easy to conclude not only that all states will in the near future not enact a compensation law, but also that if the advantage seems to be with those states which do not have such stringent laws, indefinite postponement will

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occur. However desirable it might be to have a national consciousness on social questions, the selfish and local interest of a community will long be sufficiently strong to prevent the enactment of legislation which will result in increased national efficiency. State lines are real divisions when industrial and social legislation is considered, and in the matter of workingmen's insurance for industrial accidents they present the greatest single problem. The theoretical justification of the insurance, its social gains, and national economic value can scarcely be doubted, but its practical application by the different states presents difficult problems. The problems chiefly center around the question of rates and the location of the costs. Does a state afford a sufficient basis for equitable and fair rate making, or in other words are there sufficient representatives of the various industries to make the accident experience in the state representative for the industry as a whole? In the second place, will it be possible for the employer who directly pays the cost of such insurance to shift it to his consumers, who are neither as a class residents of the state nor are compelled to buy his products? It is a social cost, or a consumer's cost, which, under a system of

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single state insurance, will be difficult to shift to him. It is peculiarly a kind of insurance suitable for state conduct, since its benefits go directly to a very large class of the population and indirectly are shared in by all of the population. Every employer has been collecting from the public sums sufficient to pay the cost of his liability insurance as an overhead expense of operation. He certainly has not consciously and willingly foregone so much of his profit, and it is not to be assumed under the prevailing conditions of competition among similar producers that he has been able to take this element of the expense from the wages of the worker. In addition to this cost of legal liability the employer may have been paying out certain sums to his workmen in case of sickness; that is, he may have continued the wages during the time of sickness or during the accident. He may also have been a liberal contributor to various organizations and funds for the benefit of the wage-earning class. A compensation law relieves him from many of these charges, and this is especially true, it is claimed, when the law is administered by the state.

In discussing or comparing costs of liability insurance or compensation insurance under private

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companies to the employer, with the costs of compensation insurance under the state, costs must be considered from a broad basis.

In the first place, the employer is relieved from paying a charge to a private company which must expect to secure a profit on the business transacted. In the second place, the compensation under the state takes care of the many cases which formerly caused the employer to make a contribution although no legal liability was incurred. In the third place, the employer is given every inducement to improve the working conditions of his plant in a manner that will reduce the number of accidents, since his rate of charge is based in part upon the injury experience of his plant. The total sums paid for direct compensation may thus be made to approach what he formerly paid for liability insurance. In the fourth place, the relatives of the injured workman, as well as miscellaneous persons, are relieved from the money expenditure which was made in such cases to care for the injured worker. In the fifth place, society is assured that the workman will receive proper care when an injury occurs, and that he will be returned in many cases to his work, whereas he formerly became a charge upon society for many

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years because he did not have proper care at the time of the injury.

In the sixth place, there is good reason to assume that fewer workmen will be injured, since under a good compensation law, and especially if it is administered by the state, the employer, the employee, and society are each interested in reducing accidents. Some support to this contention is claimed from the experience in Ohio. The accident record of those employers insured with the state under the compensation law was in 1912 one accident for each two and one half million dollars of pay roll, while those employers not so insured had one accident for each seven hundred and fifty thousand dollars of pay roll. It should be stated, however, that those insured with the state were probably the better risks. The law had not been in force sufficiently long to make great changes in the conditions of the plants, but because a premium was placed upon plants with good working conditions by a low rate the state secured the better plants.

Finally, it may be pointed out, that under a compensation law administered by the state, the large sums spent in legal proceedings would be saved. From the purely social viewpoint, which must

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be emphasized in discussing workmen's insurance, these legal expenditures represent waste. Although it does not seem to be an astounding statement to state that when the worker is injured, he is injured, yet the procedure in the past after such injuries have been suffered shows that the truth of the statement has not been accepted. Nevertheless, the social significance of the fact is that one of the members of society is disabled, and further that he should have immediate care instead of having a long drawn-out court proceeding to determine if he was injured and who is to blame for the injury.

The cost of compensation might therefore be much greater than liability insurance and yet be cheaper. Even the immediate cost to the employer might be greater than the former cost of his liability insurance, and yet in a series of years be cheaper to him in dollars and cents.

It is often urged by those opposed to extending the functions of the state that all the good results of workingmen's compensation legislation can be secured by permitting the employer to purchase this insurance from private companies. Many favor the principle of compensation but oppose the plan of having the state provide the protection.

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It is urged that this is an unnecessary interference with private business; that inefficiency in conducting the work will result from the assumed fact that the administrators of the law will be influenced by practical politics; that the cost of transacting the business will therefore be very great and more than equal whatever profit the private company would secure.

On the other hand it is contended that workmen's compensation insurance furnished by private companies would afford an opportunity or excuse for the private company to exact a high charge; that there would be no means of limiting the profit of such companies or in limiting the charge; that competition would not afford a safe protection because one result of such competition would be a "cutting" of rates by the private companies as a means of securing the business, as has often been the case in private liability insurance; that the result of this would be that the adjusters of the companies would attempt to settle claims for less than the sum provided in the compensation law in order to secure a profit for the company which had been jeopardized by writing the business at an unprofitable rate. In other words it is urged that the private company, and almost equally the

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employer, would have the same inducement to keep the workman from securing his award under a compensation law by private companies as they had under a system of employer's liability insurance.

The state, in order to prevent this result, would be compelled to employ a large number of inspectors to secure the intended operation of the law.

Neither private liability insurance companies nor employers can be criticized for the past conditions under which the employee received so little indemnity in the event of an industrial accident. The insurance company was employed by the employer. It was his servant against the employee. It did what it was paid to do, and the less it paid out, the less the employer was forced to pay in. Nor is it true that neither the private insurance company nor the employers ever did anything to aid and protect employees, but it is true that the contract made between them was a purely business contract, made for the two parties interested in it—the company and the employer.

But under a system of compensation by the state, it is claimed that no individual, company,

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class, or group has anything to gain in attempting to prevent the injured workman from securing indemnity for the accident. It is manifest that experience alone can prove or disprove many of these contentions.

CHAPTER VIII

THE RELATION OF THE STATE TO SICKNESS, OLD AGE, AND UNEMPLOYMENT INSURANCE

IT is, however, not only industrial accidents to which the wage earner is exposed, but also to the contingencies of sickness, old age, and unemployment. The question arises as to the extent to which the state should protect him against these risks.

It is probable that sickness carries with it much greater loss to society than do industrial accidents. Sickness means not only a temporary loss of employment for many workers, and hence the loss of a productive force for society, but it also means that this sickness may so undermine physical vitality that either the individual's life is shortened or he becomes a charge on society during many years of later life. The social interest in preventing sickness and in devising means of distributing the loss which it entails is evident. In the United States

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it is estimated that about 3,000,000 persons are seriously ill all the time, and of this number 900,000 are males fifteen years of age and over. If the insurance principle is to be used to protect against this contingency of illness by action of the state, there is the choice between a voluntary and a compulsory method.

An objection always urged against any action on the part of the state in this particular is that sickness is a strictly personal matter, and therefore should be provided for by the individual. Several replies may be made to this contention. In the first place many wage earners do not receive a wage from which a surplus is left, after providing the necessities, to purchase the protection against sickness. In the second place, even if the wage does make such a surplus possible, many of them, from lack of thrift and imagination, would not voluntarily provide for sickness. In their self-confidence they think the period of sickness is too indefinite and will befall some other wage earner. In the third place, society now provides for the wage earner in times of sickness, however moderate and insufficient the provision may be. Hence a charge is now borne. While the risk of sickness exists, yet this risk for the wage earner is more

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definitely connected with his work, and he is more helpless in preventing it. Many are forced to work under unsanitary surroundings. They are exposed in the crowded quarters to infectious diseases. Their food is often unwholesome and their clothing often insufficient. But a distinction, however slight in many cases, must be made between the obligation of wage earners to provide sickness and industrial accident insurance. The latter is clearly a social charge which should not in any part be borne by the wage earner except as a consumer. Society is not, however, so completely responsible for sickness, since it does not have complete control over its causes. Then, too, society must be greatly interested in encouraging and stimulating all its members to live more hygienically, to adopt habits of clean and wholesome living, and to become thrifty. These stimuli may in part be supplied by compelling the wage earner to pay a part of the cost of sickness insurance. There would also seem good reasons, both on the ground of theory and economy, to make it a state monopoly. Certainly it is a source from which private individuals should not be permitted to take profit. Yet the collections or payments for the insurance would need to be made by the state

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through the employer from the wage of the employee. As a matter of practical administration the insurance against sickness for wage earners can easily and economically be applied in connection with the industrial accident insurance. It is, in fact, a part of social insurance which is not easily separated from industrial accident insurance. The employer, as in Germany, might also be assessed a part of the cost and the remainder be contributed directly by the state from general taxation, since the prevention of illness is a subject of general concern. Yet the same practical objection to its application by a state would arise as in the case of the industrial accident insurance. There would be the same difficulty of shifting the costs from the producer to the consumer, although the necessity to do so would not be as great as in the accident insurance, since the particular state might very directly benefit from a plan of sickness insurance applied only in the state. However, confusion would almost certainly result from the diverse plans of the various states, which differently affected costs to the producers. The opportunities for economy in applying the insurance plan through a state monopoly rather than by private companies would be as great as in indus-

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trial accident insurance. The savings in agency expense under a state monopoly of compulsory sickness insurance would probably be large, as well as the savings from overhead expense of operation. Some difficulty might arise in the determination of rates, since the amount of sickness is a function of age, constitution of the population, climatic conditions, and character of the industrial life. That is to state, the cost in one state as compared with another might be much higher per capita, and the state might not afford a proper basis for the determination of rates.

The problem of old-age insurance has been well stated by G. W. Squiers in his book on "Old Age Dependency" in the following words: "Actuaries tell us that out of one thousand men living at the age of twenty, five hundred will still be living at the age of sixty-five. Economists and statisticians tell us that of the living at the age of sixty-five, two hundred will be in want and that eight ninths of all the pauperism in the country is among people who have passed the age of sixty-five." The essential social and economical problem arising is not what shall be done with this large number of dependent old, but what can the state do to reduce the number who become depend-

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ent. Neither the public almshouse nor private charity correct the condition. They only relieve the situation. Shall the state institute a system of old-age pensions to prevent these large numbers from reaching the age of destitution when they become a burden to the state? Should it establish a system of self-maintenance in old age from the contributions on the part of the industrial worker? Thus arise the two plans. One, a system in which the state makes the full contribution, and the other in which the small annual contributions are made by the wage earner during his productive years. The theory of the first plan is that the wage earner does not receive a full return for his labor under the competitive wage system, and society in his old age pays him this difference in the form of an old-age pension. It is given, not as a matter of charity, but as a payment for service rendered during the productive years. It is a deferred and contingent additional compensation for past services. In the second plan, it is said that whatever pretense is made that the pension is a payment for services rendered, the real effect is to discount thrift on the part of the wage earner and make him the recipient of a charity which injures his self-respect, and by producing

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a feeling of parasitethip, greatly reduces his potential social and economic efficiency. Yet, however desirable it may be for the wage earner to set aside a fund for old age, the actual realization of such a thing is impossible for many. Whether this is a result of lack of thrift or a result of receiving an unjust wage is immaterial for the purpose of discussing the place of the state in a system of old-age insurance.

The system of providing such insurance presents no difficulty from an actuarial standpoint, and hence the state need not hesitate to assume the business for this reason. The number reaching a certain age can be accurately determined as well as the sum necessary to be collected to pay the old-age pensions. Nor need there be much doubt that the state could transact the business at a greater economy than private companies, if it were made compulsory. Nor is there any doubt of the social value of old-age insurance. The Massachusetts Commission of 1910, which investigated the subject, estimated that the cost in that year of maintaining the dependents of sixty-five and over would be for the United States \$178,899,968. For Massachusetts alone it would be \$6,180,406. The sum which would be required under a state

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old-age pension scheme would depend upon the character of the law, as to eligibility, the amount paid, and the age constitution of the population of the state. Some very practical difficulties might arise in the application of a scheme of state compulsory old-age pensions. First, as to the source of the funds to pay the pensions. Should a period of residence be required, and if so, how long? Unless this were true, would not a state be burdened with a large number of the aged from the other states? If the state does not pay the total cost, should it be assessed upon employers in part and in part on the employees? Would an employer be able to shift to the consumer of his product the cost of this contribution if other states did not have a similar law? Might he not be forced to take from profits, if they existed, or be induced to try to get it from wages? If the employee contributes, what becomes of his contribution when he removes to another state? Would his wage be sufficient to make the contribution? Would he be willing to permit it to be taken from his weekly wage, when in an adjoining state he could receive his full wage to use as he pleased? These and many other practical difficulties would need to be solved before the states in the United

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States could enter upon a plan of old-age insurance.

The subject of Unemployment Insurance by the state introduces a problem differing very greatly from that considered in the previous forms of insurance. The appeal made to the socially minded is equally as strong for unemployment insurance as in the other cases, but the solution of the problem is infinitely more difficult. Instances of no work for the willing worker appeal strongly to our sympathy. To have a dependent family with no opportunity to earn a wage to support them is a hardship. Society is interested in having the worker earn his wage, not only to escape the burden of supporting him and his dependents, but also because of the indefinite but none the less powerful effect which it has upon social and industrial efficiency. But does a system of unemployment insurance afford the remedy? This calls for a brief reëxamination of the insurance principle. Among the several requisites for an application of the insurance principle the following are pertinent to our discussion. There must be a risk which appeals to those interested as being worth providing against. To this risk large numbers must be exposed. The risk must

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be capable of being calculated with some degree of certainty. The nature of the risk must be clearly specified. In neither of the last two particulars does unemployment fulfill the conditions. The statistics of unemployment are not sufficiently accurate to base a scientific system of insurance upon them, and unemployment itself can neither be accurately specified nor its amounts calculated on account of the various conditions of unemployment and the numerous uncontrollable forces which produce it. It is impossible to state what work each is able to do, or what work he should do and under what circumstances he should be forced to work in case of unemployment. Unemployment may be due to the workman's fault; it may be due to a strike or a lockout in the plant in which he works, or in a related plant or an industry. It may be due to industrial depressions or financial stringency, the occurrence of which cannot be predicted. It may be due to such chance elements as war, climate, or fires. Scientific insurance can only be applied when the initial risk is calculable and its future degree is also known to an accurate extent. Whatever plans are in practice among trade-unions and other organizations are not based on any scientific insur-

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ance principles. They are but mutual agreements to pay certain sums in cases of unemployment, without any reference to the particular source of the funds or their recipients. Another objection to unemployment as a plan of social improvement is that it is not essentially a method of correcting an economic and social evil, but is simply a method of relief. Unemployment in itself is an evidence of a defective economic organization. Relief may frequently tend to weaken the recipient of it.

A distinction must be made between assistance to the unemployed and unemployment insurance. The insurance plan, if it is placed in operation, gives a legal right to the assistance, while the former is based upon an expectation of relief from a purely mutual or social arrangement. Insurance could not be based upon the caprice of the human will, and yet unemployment might arise from this source. A worker might stop work, not because of unsatisfactory wages, long hours, unsanitary surroundings, but on account of the personal character of his employer. He might join with his fellow-workmen in a strike to secure justifiable improvements in wages or conditions of work. He might strike while working, and the

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employer would declare a lockout, leaving the worker unemployed. Yet all the evils of unemployment might result regardless of the reasons of the unemployment. It is the unemployment which brings the evil to be provided against, and not the causes of the unemployment. The problem of finding a method of applying the insurance principle to unemployment is therefore very great. While the risks of unemployment in the different industries cannot be accurately calculated, yet this is not a vital objection if the insurance is considered purely on its social basis. All social insurance is mutual and involves the distribution of a risk that is primarily individual. The effect of applying this principle would be to throw upon the regular trade the risks of unemployment in other trades. It would also probably be necessary to collect a part of the funds for such insurance from the employer.

The difficulty of applying a system of unemployment insurance in a state as a monopoly would be very great. Not only would all the theoretical objections to such a distortion of the insurance principle prevail, but the practical difficulties of state boundary lines would exist. The states differ very greatly in the character of

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their industrial life. Unemployment is much more common in some states than in others, and a system of unemployment insurance might be a haven of refuge for the habitually or even acutely unemployed.

There remains then to summarize the discussion of the benefits of social insurance and the obstacles to the application of such insurance in the states of the United States. In the first place Germany affords an example of the effects of a fairly wide application of social insurance. It has been in operation almost a generation in some of its forms, and hence its benefits can more accurately be known. Social Insurance is peculiarly characterized by the fact that its effects can only be known after a long series of years. Social and economic improvement among a people is only shown after time has elapsed to alter the character of the individual. In Germany social insurance commands the approval of all classes by its results. It has produced a powerful effect in the normal and material life of the German people and has doubtless had not a little to do in bringing to the Germans that reputation which they have for industrial efficiency. In the second place, a system of social insurance makes possible the improve-

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ment of the conditions of work. This expresses itself in the form of protective devices to prevent injuries, the invention of methods of reducing the loss of life in dangerous trades, the improvement in the sanitary and hygienic surroundings of the worker in the factory and the home. It tends to reduce excessive hours and application for the worker. It popularizes scientific knowledge in regard to health. It increases the efficiency of the worker, not only because it protects his health, but also because it increases his length, as well as his breadth of life. It relieves him of the worry connected with temporary or permanent disability and of old-age dependency. Nor are the purely moral effects lacking. It is a powerful factor in producing a better feeling on the part of the worker toward his employer and society. The self-respect of the worker is preserved by a realization of the mutual relationship of worker, employer, and society. No class is under the system benefiting from the misfortune of another class, but each joins with all others to bear a common burden.

It has not in Germany produced any burden upon the industrial and commerical advance of the nation, but has undoubtedly accelerated it. If the effects of Social Insurance are then so dis-

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tinctively social, the reasons for making it state insurance rather than private insurance would seem to be strong. It is a state need, and what is primarily a matter of public concern should not be used as a source of revenue for individuals.

The particular advantages of the state assuming the business would be: (1) The state could offer an absolute security and certainty which would sometimes not be present if it were in the hands of private companies. (2) The state could secure economies that would not be possible under a system of private insurance. These would consist in the collection of smaller revenue, in a reduction in the agency expense, and in the operating or management expenses, and finally in the absence of any profits. (3) The state, by assuming all the business rather than having it transacted by many private companies, would be able to attack the difficult actuarial problems in a system of social insurance, with the result that rates for the different kinds of insurance and the different classes of contributing members would be more equitable. The statistics could be economically and more accurately collected. (4) Under a system of state insurance voluntary organizations for this purpose could be preserved and encouraged.

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A system of State Social Insurance should be devised only to provide minimum insurance, and the recipients should be encouraged to use the insurance principle to provide by mutual associations additional insurance.

Yet with all these undoubtedly good results and promises in prospect under a system of Social Insurance by the state it is difficult to apply it in the states of the United States. It is easy to become so enthusiastic over the excellent social results promised in view of the deplorable conditions existing among the wage-earning classes that no sympathy or patience with the objectors to its practicability can be felt. The very name attached to this form of insurance — Social — should impress one that it is applicable only to a social and industrial unit. Yet our separate states do not afford an example of such units. The fact that it has received a modified application in some states in the form of state industrial accident insurance, and that it has placed no evident hardship on the state nor that unworkable features appear in it, is not final evidence of its success. Its results can only be told after a series of years. The laws have been in operation only a few years in the states of the United States.

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No system of State Social Insurance should be desired which does not leave a wide field of operation for voluntary insurance plans among the wage earners and between them and their employers. Mutual societies should be encouraged, and the state should, by a system of established requirements and inspections of such organizations, provide for their perpetuity. Some enthusiastic social reformers forget that the basic principle of social insurance is to provide minimum insurance. The development of thrift and individual responsibility among wage earners is no less a subject for state concern than relieving them of these misfortunes, endured in a large part for the benefit of society. But no magic power resides in the impersonal state. No enduring and efficient society has ever existed, except as the individual members composing it exemplified social efficiency. Attaining social, industrial, and intellectual excellence is very largely an individual matter. If a method can be devised of enacting a federal law for such insurance, its good results can scarcely be doubted. If such a law were passed, making uniform and compulsory provision for industrial accidents and sickness, and the states were intrusted with the administration of the law, the collection of the

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funds, and their payments to the beneficiary, few of the difficult problems of the system under the states would result. Producers would be left in the same situation as before the passage of the act. There would be no inducement in the law for the transfer either of capital or of labor. Each competitor would, so far as the provision of the law is concerned, remain as strong or as weak a competitor as he was before the enactment of the law. What was an industrial and social benefit for the nation would be nationally applied. The common welfare would be promoted by this general agency for social and industrial efficiency. In the absence of such a law the application of the principle in view of past experience will be difficult. Some states will delay the enactment of the principle, and among those which provide the insurance great difference in the laws will be found.

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